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# In the
# Supreme Court of the United States

OCTOBER TERM, 1974

No. 74-1225

THEODORE MESSNER and
MARGARET MESSNER,

*Respondents*

*vs.*

BYRON L. DORGAN, NORTH DAKOTA
STATE TAX COMMISSIONER,

*Petitioner*

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## PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF NORTH DAKOTA

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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1974

NO. _____

Theodore Messner and
Margaret Messner,

Respondents,

vs.

Byron L. Dorgan, Tax
Commissioner for the
State of North Dakota,

Petitioner.

PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF NORTH DAKOTA

Byron L. Dorgan, Tax Commissioner for the State of North Dakota petitions for a Writ of Certiorari to review the opinion and judgment of the Supreme Court of the State of North Dakota, entered in this case on December 31, 1974.

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Submitted as a separately bound Appendix transmitted with this Writ of Certiorari to the Supreme Court of the State of North Dakota

## OPINIONS BELOW

The opinion of the Supreme Court of the State of North Dakota, issued on December 31, 1974, has not as yet been reported, but will appear in _____N.D._____, _____NW 2d_____, (S.Ct. 1974). A copy of said opinion is marked Appendix A and is submitted herewith and included in the separately bound Appendix transmitted with this Petition. The opinion contains the majority opinion, one opinion concurring in part and dissenting in part, and one dissenting opinion. A Petition for Rehearing waa filed with the Supreme Court of the State of North Dakota on January 14, 1975. The North Dakota Supreme Court Denied a Petition for Rehearing on January 31, 1975, also not reported. The Court, on January 31, 1975, also issued a minute order changing some of the language in the original syllabus of the Court's opinion and decision as issued on December 31, 1974, a copy of this Order being submitted separately as Appendix B. A second minute order was issued by the Court on February 5, 1975, withdrawing the changes made to the original syllabus by the first minute order and substituted in place thereof other changes to the original syllabus. A copy of this second minute order is submitted separately as Appendix C.

The opinion of the District Court of the Fourth Judicial District of North Dakota, issued on January 8, 1974, and the Judgment of the Court as issued on January 17, 1974, are unreported and are reproduced and submitted herewith as Appendix D-1, D-2 and D-3 in the separately bound Appendix transmitted with this Petition.

The Tax Commissioner's Return to the Remand Order of the District Court of the Fourth Judicial District of the State of North Dakota, dated November 6, 1973, has not been

reported. It is reproduced and submitted herewith as Appendix E in the separately bound Appendix transmitted with this Petition.

The opinion of the District Court of the Fourth Judicial District of the State of North Dakota, dated July 3, 1973, wherein the Court remanded the case to the North Dakota State Tax Commissioner has not been reported. It is reproduced and submitted herewith as Appendix F in the separately bound Appendix transmitted with this Petition.

The Findings of Facts, Conclusions of Law and Decision of the Tax Commissioner of the State of North Dakota issued on November 22, 1972, following an Administrative Hearing conducted, pursuant to North Dakota statutes, on December 14, 1971, has not been reported. It is reproduced and submitted herewith as Appendix G in the separately bound Appendix transmitted with this Petition.

## JURISDICTION

The Judgment of the Supreme Court of the State of North Dakota was entered on December 31, 1974 (Appendix A). A timely Petition for Rehearing, filed on January 14, 1975, was denied on January 31, 1975. Minute orders of the Court were issued on January 31, 1975, (Appendix B) and February 5, 1975, (Appendix C). The jurisdiction of this Court is invoked under 28 USC §1257(3). This Petition for Certiorari is filed within the permissible ninety day period.

## QUESTIONS PRESENTED

1. Is the federal self-employment tax law an integral part of the federal income tax law to the extent that earnings, in order to be considered to be the self-employment income of the husband, must first be considered the income of the husband for federal income tax purposes, even though the income, or earnings, are derived from property owned jointly by a husband and wife?

2. Where a husband and wife derive income from jointly owned property do they have the option to report all the income therefrom as the net earnings of one spouse for self-employment tax purposes, and at the same time be able to claim that same income as the income of both, with each spouse being entitled to report one-half of those same net earnings as his or her separate income for federal income tax purposes in filing either a joint or separate income tax returns?

## STATUTES, ORDERS AND REGULATIONS INVOLVED

This case involves the following federal statutes which are reprinted in pertinent part in Appendix J submitted herewith as part of the separately bound Appendix transmitted with this Petition.

26 USC 1401(a) Imposition of self-employment tax

26 USC 1402(a) Definition of net earnings from self-employment

26 USC 1402(a)(5)(A) Income under community property laws

26 USC 1402(b) Definition of self-employment income

26 USC 1402(c) Definition of trade or business

26 USC 6012 Persons required to make returns of income

26 USC 6017 Self-employment tax returns

## STATEMENT OF THE CASE

### A.-FILING OF THE FEDERAL AND STATE INCOME TAX RETURNS

Theodore Messner and Margaret Messner are husband and wife who own several hundred acres of North Dakota farmland in joint tenancy. In 1971, they filed a joint federal income tax return, Form 1040, for the calendar taxable year 1970. In reporting for 1970 federal income tax purposes, on their joint return Form 1040, the Messners' reported net farm income in the amount of $12,363.33, plus income from interest on joint savings investments of slightly more than $1,000.00. Federal income tax was computed on a taxable income of $10,606.80, which tax amounted to $1,953.50, plus a tax surcharge computed in the amount of $49.00. As part of the joint federal income tax return, Form 1040, filed for the year 1970, there was included a self-employment tax return, Form 1040SE, filed in the name of Theodore Messner only, on which all of the net farm income, totaling $12,363.33, was reported as the self-employment income of Theodore Messner with self-employment tax being computed for Theodore Messner only on the maximum amount allowable, $7,800.00. The self-employment tax, in the amount of $538.20 was added to the amount of income tax due and owing and the total amount of $2,540.70 was remitted with the return when filed.

For the same taxable period the Messners filed separate individual state income tax returns with the State of North Dakota, whereon they divided the net farm income and the interest from the joint savings investments equally between themselves and each reported such income as their respective individual income. Attached to each of the individual state income tax returns was a statement of

"Husband and Wife Relative to Income from Farm Land held in Joint Tenancy Ownership." This statement is reproduced and submitted herewith as Appendix H in the separately bound Appendix transmitted with this Petition.

B.-THE ADDITIONAL ASSESSMENT AND PROTEST

The State Tax Commissioner of the State of North Dakota is the Petitioner filing this Petition for Writ of Certiorari to the Supreme Court of the State of North Dakota. The Tax Commissioner is charged with the administration and enforcement of tax laws of the State of North Dakota codified under Title 57 of the North Dakota Century Code, including in particular, Chapter 57-38 thereof, entitled Income Tax. Pursuant to the provisions of Chapter 57-38 the Tax Commissioner made a determination of additional state income tax due from Theodore Messner and his wife, Margaret Messner, for the taxable year 1970, and issued an assessment and mailed a Notice of Additional Tax Due to the Messners on September 1, 1971, contending that the federalizing of the state income tax laws provided that when a husband and wife who owned property in joint tenancy and derived income therefrom via the operation of a farm or some other trade or business, that the reporting of such income on a joint federal income tax return wherein the husband claimed all the income from the jointly owned property as his income so as to qualify him for the payment of self-employment tax and a self-employment tax was in fact paid by him to the Internal Revenue Service, that all the income from the jointly owned property must be considered to be the income of the person claiming it for self-employment tax purposes and that thereafter such income could not be divided between husband and wife for state income tax purposes. The taxpayers,

Theodore and Margaret Messner, filed a protest and objected to the assessment of the additional tax asserting that the federal rules to the Internal Revenue Code required the husband to claim all the income from jointly owned property as his income for self-employment tax purposes and that not withstanding the federalizing provisions of the North Dakota income tax law and the method in which the income had been reported for federal income tax purposes that the income could nevertheless be divided between the taxpayers, husband and wife, for state income tax purposes, and thus reported separately by them on individually filed state income tax returns. North Dakota is not a community property state but does recognize and provide for joint tenancy ownership.

C.-FEDERALIZING OF STATE INCOME TAX LAWS

Prior to 1967 the starting point for the computation of North Dakota taxable income for state income tax purposes was federal adjusted gross income.

In an effort to make a provision for state income tax laws to conform with the recommendations of an attorney general's opinion of June 17, 1964, the Fortieth Legislative Assembly of North Dakota enacted Senate Bill 276 (S.L. 1967, Chapter 453, Section 1) which in essence provided that even though a husband and wife filed a joint federal income tax return, separate state income tax returns could be filed wherein the separate income of each could be reported in the same way that their separate income would have been required to be reported on separate federal income tax returns. Subsection 2 of section 57-38-31 of the North Dakota Century Code, being the codification of the aforementioned legislative enactment is reproduced and submitted herewith as part of Appendix

I in the separately bound Appendix transmitted with this Petition.

During the same Fortieth session of the North Dakota Legislative Assembly and enacted after the enactment of Senate Bill 276 (S.L. 1967, Chapter 453, Subsection 1), referred to above, the concept of federalizing state income laws was changed. That is, effective for taxable years beginning on or after January 1, 1967, federal taxable income as defined and computed pursuant to the provisions of the Internal Revenue Code of 1954, as amended, would be the starting point for the computation of state income tax by all taxpayers filing North Dakota state income tax returns (Senate Bill 393, S.L. 1967, Chapter 446). The Declaration of Legislative Intent was codified as Section 57-38-01.1 of the North Dakota Century Code and this section is reproduced and submitted herewith as part of Appendix I in the separately bound Appendix transmitted with this Petition.

In reference to and in furtherance of Sections 57-38-01.1 and 57-38-31(2) of the North Dakota Century Code, referred to above, the North Dakota State Tax Commissioner promulgated Rule 57-38-050, effective July 1, 1970, entitled, Reporting of Income by Husband and Wife. Subsection 4 of Rule 57-38-050, as well as subdivision b of subsection 4 of Rule 57-38-050 are reproduced and transmitted herewith as part of Appendix I in the separately bound Appendix transmitted with this Petition.

D.-THE RESULTS BELOW - SHOWING HOW FEDERAL QUESTION WAS RAISED AND PASSED UPON

In making the determination of additional state income tax due and issuing the Notice and Assessment the State Tax Commissioner contended that the taxpayers in filing

separate state income tax returns had to conform with the provisions of the federal Internal Revenue Code of 1954, as amended, as they applied to the filing of separate federal income tax returns by a husband and wife who each had separate income. Therefore, the fact that the husband had claimed all the income from the farming operation as his self-employment income so as to qualify himself for self-employment tax purposes also made it his income for income tax purposes on either a joint federal or separate federal income tax return. This being so because the self-employment income tax return is part of the federal income tax return and before a taxpayer can report income as self-employment income he must show and declare income that is his and his only for income tax purposes. There can be no assignment of income.

In the Findings of Facts made by the Tax Commissioner on November 22, 1972, following an Administrative Hearing conducted on December 14, 1971, and transmitted herewith as Appendix G, it was found that all the net income from the operation of the farm unit was treated as the income of Theodore Messner, qualifying him for federal self-employment tax purposes, and that Theodore Messner paid self-employment tax on the maximum amount permissible. The Conclusions of Law issued by the Hearing Officer on November 22, 1972, (Appendix G) state that a husband and wife filing separate state income tax returns must report their separate income in the same way that their separate income would have been required to have been reported if separate federal income tax returns were filed. Further, the conclusion was asserted that the starting point for state income tax purposes was taxable income as computed pursuant to the provisions of the United States Internal Revenue Code of 1954, as amended. Still further, the conclusion was made that a

husband and wife in filing a joint federal income tax return wherein the income from jointly owned property is considered the income of the husband so as to qualify the husband for self-employment tax coverage and who then report this income as the husband's self-employment income for self-employment tax computation, cannot thereafter claim this same income to be other than the husband's when filing state income tax returns. In the Decision, Appendix G, the Hearing Officer ruled that in arriving at federal taxable income when preparing a federal income tax return, the provisions of the federal income tax law pertaining to what is income and what are deductions must be followed. Further, that the income of Theodore Messner had always been considered and treated as his income for federal income tax purposes so as to qualify the income as his self-employment income.

On appeal to the District Court of the Fourth Judicial District of North Dakota, Appendix F, the Judge on July 3, 1973, in remanding the matter back to the Tax Commissioner's administrative hearing for the taking of additional evidence, stated that the Court found that the declaration of self-employment income was not conclusive upon the declarant or his spouse unless the presumption that it was the income of the husband was overcome.

The Tax Commissioner's return to the remand order of the District Court, Appendix E, dated November 6, 1973, made the additional finding that there had been no express showing, either during the time that the income from the jointly owned property was being earned, or at some point of time after it was earned, that the income was the income of someone other than the husband's, Theodore Messner, and that it was other than his for

federal income tax purposes so as to qualify this same income for the husband's self-employment tax purposes.

The opinion of the District Court of the Fourth Judicial District of North Dakota was issued on January 8, 1974, Appendix D-1, and stated that sufficient evidence had not been received to rebut the presumption that all of the income from the jointly owned property was that of the husband, particularly in light of his declaration of taxable income for qualification for federal self-employment purposes. In the Judgment entered on January 17, 1974, Appendix D-2, the Court judged and determined that the Decision and Determination of the State Tax Commissioner as entered on November 22, 1972, be in all things affirmed.

On Appeal, the North Dakota Supreme Court on December 31, 1974, Appendix A, ruled that the federal self-employment tax is a part of the social security system and not a constituent part of the federal income tax, although self-employment tax returns are filed with personal income tax returns for administrative convenience. The majority of the Court in its opinion stated that they believed the Tax Commissioner was in error in considering the self-employment tax as a part of the federal income tax. This belief being based on the provisions of 26 U.S.C. 1401 and 1402, imposing the tax and defining net earnings from self-employment, and §6017 of the Internal Revenue Code, imposing a duty to file a self-employment tax return if an individual has self-employment earnings of $400.00 or more, irrespective of whether an income tax return is required under §6012 IRC. The Court also made an interpretation of §§1401 and 1402 of the Internal Revenue Code. The majority stated in the opinion that the exercise by a taxpayer of the option to claim income

from property jointly owned with his wife as to self-employment tax had no bearing upon his (or her) income tax liability, state or federal, and did not justify the Tax Commissioner's treating that election as conclusive for state income tax purposes. Further, the Court said that if the self-employment tax is a separate federal tax, and not a part of the federal income tax, then spouses who jointly own property may elect to report the joint income from that property jointly for federal income tax purposes and separately as to one spouse for self-employment tax purposes. In discussing 26 USC 1402(a)(5)(A) the Court stated that the Internal Revenue Code makes no provision whatsoever for the resolution of similar questions arising in states which do not recognize community property, such as North Dakota, but that the provision as to community property states is an indication that the federal authorities consider an election as to self-employment income to be irrelevant as to the right to file joint or separate federal income tax returns; and that therefore the state should likewise consider it irrelevant as to the right to allocate income from jointly owned property on state tax returns.

The federal questions sought to be reviewed here were raised in the administrative proceedings and in the state District Court and in the North Dakota Supreme Court. Because of the federalizing of the state income tax laws the state courts must apply the interpretations of the federal Internal Revenue Code to state income tax matters, and in those instances when the federal statutes must be interpreted, an incorrect interpretation by the State Court of law is subject to review by the United States Supreme Court. Rule 19 of the Rules of the United States Supreme Court in subdivision (a) of subsection 1 states one of the

pertinent considerations governing review on certiorari -

> "Where a state court has decided a federal question of substance not theretofore determined by this court, or has decided it in a way probably not in accord with applicable decisions of this court."

## REASONS FOR GRANTING THE WRIT

1. The question presented is of importance to taxpayers in income tax planning and in estate planning and in the administration of the North Dakota state income tax laws.

Settlement of the question by this Court is in the public interest. Theodore Messner and his wife, Margaret Messner, are representative of many North Dakota taxpayers who are confronted with the same problem. North Dakota has a total population of approximately 625,000 people who file some 225,000 income tax returns yearly with the Tax Commissioner's office. Of these, some 47,000 returns are presently received from married couples filing separate returns, each having separate income to report. It is noted by department statistics that this figure is increasing with every filing period. More pertinent is the statistic that out of the 225,000 returns some 43,000 are received from farmers, and in North Dakota a bulk of the farm property is in joint tenancy. In 1973 some 4,200 married couples who were engaged in farming filed separate returns. Following the decision of the North Dakota Supreme Court in the Messner matter this number will increase significantly in the future (1974 returns now being filed indicate close to 50% of all farm returns will be separate filings) thereby possibly subjecting these same taxpayers to audit by the Internal Revenue Service because of the fact that the wife has not paid self-employment tax on the self-employment income which she claimed as hers from the jointly owned property when she filed state income tax returns.

It should be noted that the problem is not limited to husbands and wives holding farm property in joint tenancy but also extends to other trades, businesses or professional activities of a husband and wife

where either all or part of the property may be in joint tenancy. Another danger that exists is that a husband and wife may put their holdings in joint tenancy in hopes of minimizing their state income tax liability, failing to recognize the pitfalls that joint tenancies may create in other businesses or domestic relationships.

2. The question presented is essentially one of interpretation and application of federal law, specifically, the Internal Revenue Code of 1954, as amended.

The Supreme Court of North Dakota erred in its interpretation and application of federal income tax statutes in holding that Theodore Messner had an "option" under the federal statutes to claim income from property jointly owned with his wife as all his income for self-employment tax purposes and then as joint income for federal income tax purposes. (Appendix A). The Court further erred in making the interpretation that federal authorities would consider an election as to self-employment income to be irrelevant as to the right to file joint or separate federal income tax returns. (Appendix A)

In applying the North Dakota Court's interpretation of the federal statutes it would be possible for a husband to claim and report all the income from jointly owned property as his self-employment income and pay the self-employment tax and receive the maximum benefits. Then, if separate federal income tax returns were filed, the income from the jointly owned property could be divided equally between them and each would then report their respective share as separately earned income. This is not a proper interpretation of federal law and is an interpretation to which the federal courts have not previously addressed themselves.

3. Decision of the Courts below creates confusion.

The Courts of North Dakota have not ruled that the state statutory provisions pertaining to this question are unconstitutional, nor have they considered the rule promulgated in connection therewith unconstitutional or to be the improper delegation, assumption or usurpation of power.

Rather, they have ruled that the Tax Commissioner has misapplied both the law and the rule as it pertains to the Messners. However, in making their determination that the law and rule had been misapplied, the North Dakota Supreme Court made an interpretation of federal statutes that was incorrect and thus erred in their application.

If the interpretation of the North Dakota Courts stands, jointly owned property of a husband and wife will be entitled to different tax treatment from that of jointly owned property of persons not husband and wife. For instance, two brothers who derive income from property in joint tenancy will not be permitted to report their respective share for income tax purposes and still be permitted to allow one of them to claim all the income for self-employment tax purposes.

4. Enactment of the self-employment tax in 1950 by the federal government should not ressurect the problems involving income from jointly owned property that existed prior to the amendments of 1948 to the Internal Revenue Code.

The 1948 Revenue Act made fundamental changes in the federal taxation of income from jointly owned property and also made it possible for taxpayers from community property and non-community property states to

enjoy the same benefits.

By permitting a husband and wife to split combined income in half for the purpose of computing federal income tax, the Revenue Act of 1948 made it possible for a husband and wife who had income from jointly owned property to report that income on a single joint return and thus take advantage of lower tax rates. This procedure made it unlikely that a husband and wife would file separate income tax returns because of the higher rates that would apply. However, if separate returns were filed, the question of who had how much income from the jointly owned property still remained and was answered by the application of the general rules, and the exceptions thereto, as to income from jointly owned property.

The enactment of the self-employment tax in 1950, while for the purpose of providing retirement income to contributing taxpayers similar in form and amount as received by those persons receiving benefits under the Social Security Act, was nevertheless enacted as an integral part of the federal income tax law. (Federal Tax Regulations, 1970, Reg. 1.1401-1:

> "This tax shall be levied, assessed and collected as part of the income tax imposed by Subtitle A of the Code . . . ."

and

> "Since the tax on self-employment income is part of the income tax . . . ."

The Self-employment Tax Act provides that an individual with self-employment income, that is, net earnings from the operation or conduct of a business or trade, must report his or her separate income for self-employment

tax purposes. There can be no appropriation or assignment of some other person's share, be it a joint property owner or what. Further, computation of self-employment income is done by first computing net income for income tax purposes. This means that before a taxpayer can have net earnings from self-employment he or she must first have income from a trade or business that in turn is exposed as such income for income tax purposes.

## CONCLUSION

The decision below is erroneous. Much time has elapsed and much effort consumed to bring the matter to this Court. The material submitted to date makes this a rather voluminous file and therefore lengthy to this Court. But the instant case raises a question of general importance in the administration of the tax laws which should be reviewed by this Court. For the reasons given we believe it is in the public interest that the Petition for Certiorari should be granted.

Dated this 26th day of March, 1975, at Bismarck, North Dakota.

Respectfully submitted,

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MAR 27 1975
MICHAEL RODAK, JR., CLERK

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BYRON L. DORGAN, NORTH DAKOTA
STATE TAX COMMISSIONER,

*Petitioner*

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# Appendix

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to

Petition for Writ of Certiorari to the
Supreme Court of the State of North Dakota

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# APPENDIX

TO

PETITION FOR WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF NORTH DAKOTA

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APPENDIX A

IN THE SUPREME COURT
STATE OF NORTH DAKOTA

Theodore Messner and
Margaret Messner, Petitioners and Appellants

v.

Byron L. Dorgan,
Tax Commissioner for
the State of North
Dakota, Respondent and Appellee

CIVIL NO. 9020

1. Presumption of law arising from Rule 50-4-b of Rules and Regulations of the State Tax Commissioner that person reporting income for Federal self-employment tax purposes claimed all right to such income with the consent of his or her spouse is rebutted by statement of both spouses under oath that no such consent was given and no such claim was made.

2. The Federal self-employment tax is a part of the Social Security System and is not a constituent part of the Federal income tax, although self-employment tax returns are filed with personal income tax returns for administrative convenience.

3. A State statute permitting allocation of income between husband and wife cannot be negated by administrative rule which purports to interpret it.

4. It is the duty of the courts to reconcile provisions of law relating to the same subject matter if possible, and particularly so when the statutes are adopted at the

same legislative session. Fact that State has partially "Federalized" the State income tax does not detract from validity of separate statute which relates to a non-Federalized area of income tax law.

5. Decision of administrative agency which is against the law or not sustained by substantial evidence will not be sustained.

(Syllabus by the Court)

Appeal from the District Court of Burleigh County, the Honorable Alfred A. Thompson, Judge.

REVERSED.

Opinion of the Court by Vogel, J.

L. A. W. Stephan, Valley City, for petitioners and appellants.

Albert R. Hausauer and Robert W. Wirtz, Special Assistant Attorneys General, State Tax Department, Bismarck, for respondent and appellee.

MESSNER V. DORGAN

VOGEL, J.

The appellants, Theodore and Margaret Messner, are husband and wife. Since their marriage in 1935, they have purchased 800 acres of farmland. The land is held in joint tenancy and was farmed by them during the year 1970.

In 1971, they filed a joint Federal income tax return for the 1970 tax year. In the return they listed net farm income of slightly more than $12,000 and income from

interest on joint savings investments of slightly more than $1,000. For the same year they filed separate State income tax returns, dividing the income shown on the Federal return between them.

As part of their Federal tax return the Messners filed a self-employment tax return in which the gross income from the farm was shown, for self-employment tax purposes, as the income of Theodore Messner. The Tax Commissioner contends that the Messners are prohibited, by statute and Tax Commissioner's Rule 50-4-b, from filing separate returns splitting income which has been allocated to one of them on a self-employment tax return. The Messners contend that Tax Commissioner's Rule 50-4-b is not authorized by statute and is invalid.

The State Tax Commissioner assessed additional State income taxes for the year 1970 against the Messners, and they appealed to the district court of Burleigh County, which, after remanding the case once to the Tax Commissioner for the taking of further evidence, affirmed the decision of the State Tax Commissioner. This appeal followed.

The dispute between the parties arises over the interpretation of Section 57-38-31, subsection 2, N.D.C.C., and the validity and application of Rule 50-4-b promulgated by the Tax Commissioner. Relevant portions of the statute and the rule follow:

> "57-38-31. Duty of individuals and fiduciaries to make return.--1. Every resident individual, every fiduciary for a resident individual, estate or trust, and every individual or fiduciary who receives income derived from sources in this state, who is required by the provisions of the United States

Internal Revenue Code of 1954, as amended, to file a federal income tax return, shall file an income tax return with the state tax commissioner in such form as he may prescribe . . . . The return shall be signed by the person required to make it and shall contain a written declaration that it is made and subscribed under penalties of perjury.

"2. A husband and wife each having separate income may include their income in a single joint return, or if they have separate income from personal or professional services or from business or property in which the other has no ownership and if they file a joint federal income tax return in which such income is reported, they may file separate returns in which the separate income of each and the deductions and exemptions for themselves or their dependents are reported in the same way that they would have been required to report them in separate federal returns if they had filed separate federal returns.

"A husband and wife who have income from property or business in which both have an ownership interest may file a single joint return in which the income of both, along with any other income they may be required to report, is included, or they may file separate returns in the same way as provided in the preceding paragraphs, provided that the income from the property or business in which both have an ownership interest shall be allocated between them according to the capital interest of each, the management and control exercised by each, and the services performed by each with respect to such property or business, pursuant to rules

and regulations promulgated by the tax commissioner for the reasonable allocation thereof.

. . . . .

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"INCOME TAX RULE NO. 50/REPORTING OF INCOME BY HUSBAND AND WIFE

. . . . .

"4. Income from a business in which both husband and wife have an ownership interest.

. . . . .

"b. Allocation of income derived from a business other than a partnership in which both a husband and wife claim an ownership interest

"In the case of a business owned by a husband and wife who filed a joint federal income tax return in which one of them claimed all of the income therefrom for federal self-employment tax purposes, it will be presumed for purposes of administering the state income tax law, unless expressly shown to the contrary by the taxpayer, that the spouse who claimed that income for federal self-employment tax purposes did, thereby, with the consent of the other spouse, claim all right to such income and that therefore such income must be included in the state income tax return of the spouse who claimed it for federal self-employment tax purposes if the husband and wife file separate state income tax

returns.

. . . . .

"d. Management and control

"Participation in the control and management of a business must be distinguished from the regular performance of nonmanagerial services. Contribution of management and control with respect to the business must be of a substantial nature in order to accord it weight in making an allocation of income. Substantial participation in management does not necessarily involve continuous or even frequent presence at the place of business, but it does involve genuine consultation with respect to at least major business decisions, and it presupposes substantial acquaintance with an interest in the operations, problems, and policies of the business, along with sufficient maturity and background of education or experience to indicate an ability to grasp business problems that is appreciably commensurate with the demands of the enterprise concerned. Vague or general statements as to family discussions at home or elsewhere will not be accepted as a sufficient showing of actual consultation, but evidence of genuine consultation with respect to specific matters is entitled to consideration even though it has taken place in the home. Evidence of genuine consultation with respect to the distribution of profits or the retention in the business is significant and to be accorded weight in determining proper allocation of income.

"e. Services performed

"The amount of services performed by each spouse is a factor to be considered in determining proper allocation of income from a business in which each spouse has an ownership interest. In order to accord weight to services performed by an individual spouse, the services must be of a beneficial nature in that they make a direct contribution to the business. For example, for a business operation, whether it is a retail sales enterprise, farming operation or otherwise, in which both husband and wife have an ownership interest, the services contributed by the wife must be directly connected with the business operation; services for the family such planting and maintaining family gardens, domestic housework, cooking family meals, and routine errands and shopping, are not considered to be services performed or rendered as an incident of or a contribution to the particular business; such activities by a wife must be disregarded in determining the allocable income attributable to the wife."

The Messners obviously were aware of the provisions of Rule 50-4-b, because attached to each of the separate individual State tax returns was the following statement:

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STATEMENT OF HUSBAND AND WIFE RELATIVE TO INCOME FROM FARMLAND HELD IN JOINT TENANCY OWNERSHIP

Taxpayers, husband and wife, have filed a joint federal income tax return for 1970 listing joint income from land held in joint tenancy ownership. Under federal regulations (See below*) husband was required to pay self-employment tax on all earnings from farm.

Wife was not permitted to claim part for self-employment tax purposes. This was not optional on the part of either.

This statement is made to set forth clearly that taxpayers on their separate state income tax returns each claims his share of income from jointly owned land, that neither has given any consent of any kind to husband's including such income in the federal tax return for self-employment purposes, and that such was done because it was mandatory under federal laws and regulations.

Dated 3/26/71

(Signed) Theodore Messner

(Signed) Margaret Messner

The Messners' quotation from the Farmer's Tax Guide is perhaps a little misleading. The full paragraph from which the excerpt is taken reads as follows:

> "Your wife is not considered 'self-employed' with respect to your earnings from self-employment, even though you file a joint income tax return. If your wife is operating her own business, whether farming or anything else, she is a self-employed person and a separate self-employment tax for her may be due. If so, her self-employment tax

*Farmer's Tax Guide - 1971 Edition: "Your wife is not considered 'self-employed' with respect to your earnings from self-employment, even though you file a joint income tax return - - - - - mere ownership, or joint ownership, of farm property does not qualify a spouse for self-employment purposes."

> should be computed on a separate self-employment tax schedule and reported with yours on line 56 of the joint income tax return, Form 1040. Mere ownership, or joint ownership, of farm property does not qualify a spouse for self-employment tax purposes."

In denying the claim of the Messners that they were entitled to split their income, as permitted by Section 57-38-31, supra, the Tax Commissioner mailed to appellants a notice of determination of assessment of additional taxes which contained the following remarks:

> "Splitting of income disallowed. See attached schedule of corrected liability. The fact that land is held in joint tenancy does not qualify a husband and wife to file separate returns, splitting income from a farming operation in half. See enclosed copy of income tax Rule No. 50-Section 4, paragraphs A, B, C, D, & E."

Before going further into the history of the litigation, we can comment at this point on two of the conflicting contentions of the parties.

On the one hand, we cannot agree with the Messners that the allocation of all the income of both spouses to the husband, so far as the self-employment tax was concerned, was "not optional" or "was mandatory under federal laws and regulations." Their claim is based upon language in the "Farmer's Tax Guide," an official publication of the Internal Revenue Service, quoted above. That publication merely says that the wife is not considered self-employed as to the husband's earnings, and that "mere . . . joint ownership" of farm property does not qualify a

spouse for self-employment tax purposes. In the absence of authoritative construction by Federal administrative agencies or courts, we read this language as covering only such instances as (1) where the husband earns all the money, as by farm labor or crop shares, or (2) where attribution of income to the wife is based solely upon co-ownership, without any labor on her part. The publication provides no guidance at all in cases such as the present one, where the husband and wife not only own the property together but work together to make it produce income. We assume that they could have divided the income for Federal self-employment tax purposes and provided the Federal Internal Revenue Service with proof of joint management and labor to produce the income and thereby justified the division for self-employment tax purposes. Of course, this would have required the payment of more self-employment taxes.

On the other hand, we cannot agree with the Tax Commissioner that the Messners did not comply with Rule 50-4-b. That rule creates a presumption that "the spouses who claimed . . . income for federal self-employment tax purposes, did, thereby, with the consent of the other spouse, claim all right to such income . . ." This presumption is to be given effect "unless expressly shown to the contrary by the taxpayer." The taxpayer showed to the contrary, in the most express way possible, by submitting a statement signed by both husband and wife saying that no such consent was given and no such claim was made. This statement was filed along with, and at the same time as, the filing of the returns upon which the Commissioner relies to establish the presumption. The Commissioner appears to construe Rule 50-4-b as creating a presumption that the husband earned all the money. Such a presumption,

as the trial court noted, would be subject to attack on constitutional grounds. But the rule, by its terms, only creates a presumption that one spouse consented to the claim of right to such income by the other spouse. We hold that this presumption was overcome.

The question remaining before us is whether the evidence submitted by the parties, without the benefit of the presumption--which was negatived by the statement of the Messners --supports the imposition of the additional tax.

In resolving this question we find that the record is not as helpful as it might be. In fact, much of the record indicates that the evidence of the Messners as to their joint participation in the earnings of the income was disregarded during most of the proceedings below.

The hearing on the protest of the Messners was held before an examiner of the Tax Department. He ruled that a husband and wife who file a joint Federal tax return allocating income to the husband for self-employment tax coverage "cannot thereafter claim this same income to be other than the husband's when filing state income tax returns." He thereby ignored the language of the statute, Section 57-38-31, subsection 2, N.D.C.C., which permits a husband and wife to file separate State returns with income "allocated between them according to the capital interest of each, the management and control exercised by each, and the services performed by each . . ." Such evidence was extensive and tended to support the Messners' claim of an equal division of income. It showed that they were very poor when they married, that they worked together in acquiring some property, that the wife not

only cooked and did the household work but assisted in the harvests, that she milked the cows, that she kept most of the farm and household records, and that she participated in the making of decisions as to purchase of machinery. The Tax Commissioner offered no evidence to contradict the testimony of the Messners on this matter.

When this case reached the district court the first time, Judge Thompson, after an extended analysis of the law and facts, came to many of the conclusions we have reached above. He held that the Messners were not compelled by Federal regulations to file a self-employment tax return in the name of the husband alone, that Rule 50 did not (and could not constitutionally) create an absolute bar to the filing of separate State tax returns by husband and wife even though one or the other had filed a self-employment tax return on the same income, and that the State Tax Commissioner should be required to consider the evidence as to the management, control, and services of the Messners. He remanded the case to the Tax Commissioner for the taking of additional evidence and the making of new findings.

The Tax Commissioner then offered the Messners an opportunity to present additional evidence. They declined to present further evidence, relying on what they had already presented. Neither did the Tax Commissioner offer additional evidence. Instead, he made new findings and a new decision. The new findings were to the effect that the Messners had not rebutted the presumption created by the filing of the self-employment tax return, and the previous ruling was affirmed.

The language of the pertinent findings, on remand, of the Tax Commissioners is as

follows:

"(C) The Plaintiffs-Appellants have not rebutted the presumption that all of the income from the jointly owned property is the income of the husband, Theodore Messner, one of the Plaintiffs-Appellants.

"(1) Section 57-38-31(2) in providing for income from jointly owned property to be allocated between husband and wife according to the capital interest of each, the management and control exercised by each, and the services performed by each with respect to such property or business applies in those situations where neither spouse has claimed all the income as his or her income when filing a federal income tax return for that same income.

"(2) The evidence submitted at the administrative hearing indicates that the wife, Margaret Messner, one of the Plaintiffs-Appellants, had some ownership interest of record and that she participated to some degree in the management and control and that she did perform some services, but the evidence submitted does not establish the fact that these activities on her part were engaged in for the purpose of claiming any part of the income from the jointly owned property as her separate income for her income tax purposes.

"(3) There has been no express showing, either during the time that

the income from the jointly owned property was being earned, or at some point of time after it was earned, that the income was the income of some one other than the husband's, Theodore Messner, and that it was other than his for federal income tax purposes so as to qualify this same income for the husband's self-employment tax purposes.

"(D) Plaintiffs-Appellants have not met the requirements of Section 57-38-01.1, Section 57-38-01.2, Section 57-38-31(2) and Rule No. 50(4)(b) in that:

"(1) Section 57-38-01.1, enacted later in time than Section 57-38-31(2), takes prescedence and expresses the intent of the legislature in that the starting point for the computation of state income tax by all taxpayers shall be federal taxable income.

"(2) Section 57-38-01.2, enacted later in time than Section 57-38-31(2), takes prescedence and provides that federal taxable income is the starting point for computing state income taxes.

"(3) Section 57-38-31(2), having been superseded, must be interpreted and construed in the light of the legislative intent expressed in Section 57-38-01.1 in that a husband and wife electing to file separate state income tax returns after filing a joint federal income tax return may do so only after they have computed their separate federal taxable income under the provisions of the United States Internal Revenue Code and each then uses this recomputed federal taxable income as the starting point for computing their state income tax.

"(4) Section 57-38-31(2), having been superseded, must be interpreted and construed both in conjunction with and subjunctive to Sections 57-38-01.1 and 57-38-01.2 in that when income from jointly owned property is reported for federal income tax purposes as the taxable income of the husband so as to qualify that income for federal self-employment purposes in the husband's name it cannot thereafter be treated in whole or in part as someone else's taxable income for state income tax purposes.

"(5) Rule No. 50, and in particular that portion referred to as Rule No. 50(4)(b), was promulgated taking into consideration the filing provisions provided for in Section 57-38-31(2) and the intent of the legislature as expressed in Section 57-38-01.1 and provided for in Section 57-38-01.2." (Emphasis added, to point out findings we deem to be erroneous.)

It appears to us that these findings totally disregard the admonition of Judge Thompson that Mrs. Messner was not estopped by her husband's declaration, for self-employment tax purposes, of entitlement to the income from the farm. The Tax Commissioner, in the face of the first ruling of the district court, with which we agree, disregards the plain language of Section 57-38-31, subsection 2, and construes that statute as applying only "where neither spouse has claimed all the income as his or her income when filing a federal income tax return for that same income." Section 57-38-31, subsection 2, contains no such limitation. The Tax Commissioner then adds a requirement to the same section of the statute when he

demands that Mrs. Messner establish that her ownership interest and participation in management and control and performance of services were "for the purpose of claiming any part of the income from the jointly owned property as her separate income for income tax purposes." There is no such requirement in the statute. The Tax Commissioner then disregards the testimony presented by the Messners in holding that there has been "no express showing, . . . that the income was the income of some one other than the husband's," and, finally, the Tax Commissioner makes a legal argument to the effect that Section 57-38-31, Subsection 2, is, in effect, repealed ("superseded") by the subsequent enactment (at the same legislative session) of Sections 57-38-01.1 and 57-38-01.2. (Section 57-38-31, subsection 2, was a part of Chapter 453, 1967 Session Laws, and Sections 57-38-01.1 and 57-38-01.2 were a part of Chapter 446, 1967 Session Laws.) Without setting forth the lengthy provisions of the latter sections, suffice it is to say that we find no conflict between them and Section 57-38-31, subsection 2.

We believe the Tax Commissioner is in error in considering the self-employment tax as a part of the Federal income tax. It is true that the self-employment tax return is filed as a part of the Federal income tax return, but it appears to us that it is a separate tax, the return of which is filed with the income tax return for administrative convenience. We base this belief on the provisions of 26 U.S.C. 1401 and 1402, imposing the tax and defining net earnings from self-employment, and Section 6017, imposing a duty to file a self-employment tax return if an individual has self-employment earnings of $400 or more, irrespective of whether an income tax return is required under Section

6012 (which requires the filing of an income tax return if one has a gross income of a considerably larger amount.) Section 1401 provides, in part:

> "In addition to other taxes, there shall be imposed for each taxable year, on the self-employment income of every individual, a tax . . ."

Section 1401 defines net earnings from self-employment as "the gross income derived by an individual from any trade or business carried on by such individual, less the deductions allowed by this subtitle which are attributable to such trade or business,. . ." with certain exclusions such as rentals, dividends, certain gains or losses, and wages. Thus both the imposition and the incidence of the tax, as well as the duty to file a return, are different from and in addition to the requirements of the Federal income tax laws. It therefore is our opinion that the exercise by a taxpayer of the option to claim income from property jointly owned with his wife as to self-employment tax has no bearing upon his (or her) income tax liability, State or Federal, and does not justify the Tax Commissioner's treating that election as conclusive for State income tax purposes. If the self-employment tax is a separate Federal tax, and not a part of the Federal income tax, then spouses who jointly own property may elect to report the joint income from that property jointly for Federal income tax purposes and separately as to one spouse for self-employment tax purposes, and they may allocate the income between them in their State income tax return as permitted by Section 57-38-31, subdivision 2, according to rules and regulations promulgated by the Tax Commissioner for the allocation thereof.

We note that the Federal Internal Revenue Code makes provision for a husband to claim all the income in a community-property State for self-employment tax purposes, regardless of the fact that the income is equally divided for income tax purposes. See 26 U.S.C. 1402(a)(5)(A). The Internal Revenue Code makes no provision whatsoever for the resolution of similar questions arising in States which do not recognize community property, such as North Dakota, but the provision as to community-property States is an indication that the Federal authorities consider an election as to self-employment income to be irrelevant as to the right to file joint or separate Federal income tax returns. We likewise consider it irrelevant as to the right to allocate income from jointly owned property on State tax returns. We note further that the self-employment tax actually is a part of the Social Security system and provides for contributions to that system by self-employed persons. In this respect also, it is different from the income tax.

Sections 57-38-01.1 and 57-38-01.2, N.D. C.C., declare a legislative intent to simplify the State income tax laws by adopting the Federal definition of "taxable income" as the starting point for the computation of State income tax and to make adjustments to that figure to arrive at a taxable income for State income tax purposes.

It is our duty to reconcile the provisions of law relating to the same subject matter if we can, and particularly is this true as to statutes adopted at the same legislative session. State ex rel. Gammons v. Sorlie, 56 N.D. 650, 219 N.W. 105 (1928). Since we believe that the Federal self-employment tax is no part of the Federal

income tax, but instead is a separate tax, we find no connection between the concept of "Federalizing" the State income tax, at least as to the starting point for the computation of the State tax, and the election made by the Messners as to allocation of their income for Federal self-employment tax purposes.

The Messners contend that Rule 50-4-b is invalid because it is beyond the authority of the Tax Commissioner to promulgate such a rule. The Tax Commissioner contends that the rule in question is authorized by the provisions of Section 57-38-56, N.D.C.C., giving him authority to "prescribe all rules and regulations, not inconsistent with the provisions of this chapter, necessary and advisable for its detailed and efficient administration,. . ." While we recognize the authority of the Tax Commissioner to make proper rules and regulations, we find that Rule 50-4-b would be unconstitutional if applied here as the Tax Commissioner applied it, so as to forbid allocation between husband and wife of income from jointly owned property if one or the other of them had claimed the income on a Federal self-employment tax return.

Although we construe Rule 50-4-b to be valid where neither spouse seeks to negative the presumption set forth in the rule "that the spouse who claimed that income for federal self-employment tax purposes did, thereby, with the consent of the other spouse, claim all right to such income," the Tax Commissioner has misapplied the rule in this case in view of Mrs. Messner's showing that she actively participated in the labor and management of the farm operation.

We find that the decision of the Tax Commissioner is against the law and is not sustained by substantial evidence in the

light of the entire record. Sec. 28-32-19, N.D.C.C.; O'Brien v. North Dakota Workmen's Compensation Bureau, 222 N.W. 2d 379 (N.D. 1974).

The Tax Commissioner vigorously asserts that we should follow the decisions of the Wisconsin Supreme Court in Stern v. Wisconsin Department of Revenue, 63 Wis. 2d 506, 217 N.W. 2d 326 (1974), and Skaar v. Wisconsin Department of Revenue, 61 Wis. 2d 93, 211 N.W. 2d 642 (1973). The cases are not in point. Wisconsin has no statute such as Section 57-38-31, subdivision 2, N.D.C.C., nor does Wisconsin allow income-splitting except through the device of a partnership. In Skaar, supra, the Wisconsin Supreme Court said:

> "While the Wisconsin income tax is modeled upon the federal system, the personal income tax treatment of married individuals under the federal and Wisconsin tax provisions is dissimilar. Under the federal system, married individuals are permitted to file a joint return and effectively split their income even though all income and deductions belong to only one spouse. Wisconsin, on the other hand, while permitting married individuals to file jointly, taxes each spouse individually on his income and deductions and income splitting is not allowed." 211 N.W. 2d 642, at 644.

Since Wisconsin has no statute allowing allocation of income between joint owners, the Skaar and Stern cases are decided solely on a determination as to whether a partnership between husband and wife existed under applicable Wisconsin law. No question of the existence of a partnership between the Messners is before us. On the contrary, we are dealing here with interpretation of a

North Dakota statute and a North Dakota administrative rule, both without parallel in the Wisconsin scheme of taxation.

Since the rules and regulations quoted in this opinion, other than Rule 50-4-b, are not attacked by the Messners, we express no opinion as to their validity, nor as to the propriety of exclusion by rule or consideration of certain kinds of contributions by a wife who is a joint owner of the property and who contributes by her labors to the production of the income.

Because no good purpose would be served by sending the matter back for further consideration by the district court or the Tax Commissioner, it having been considered twice by each, we reverse and remand for entry of judgment in favor of the Messners.

/s/ Robert Vogel
/s/ Harvey B. Knudson
/s/ Ralph J. Erickstad, C.J.

Messner v. Dorgan

JOHNSON, J., concurring in part and dissenting in part.

I am in agreement with the analysis made by the majority opinion, particularly as it relates to the Commissioner's position that the regulation in question creates some form of irrebuttable presumption. However, I believe the appropriate remedy to be a remand for additional proceedings before the Tax Commissioner under the Administrative Agencies Practice Act. There has been a disagreement as to the legal effect of the regulation and the statute relating to income from jointly owned property. As that

question has been resolved by the opinion of this court, a factual determination should be made of the income allocated between the husband and wife according to the capital interest of each, the management and control exercised by each, and the services performed by each with respect to such property. See §57-38-31, N.D.C.C.

Questions of fact are properly determined before the administrative agency where there is opportunity for the presentation of evidence and the examination and cross-examination of witnesses. See §§28-32-13 and 28-32-19, N.D.C.C. While there have been previous proceedings before the Tax Commissioner, the question has not been considered in the legal framework established by this opinion.

/s/ J. Philip Johnson

Messner v. Dorgan

PAULSON, Judge. (Dissenting)

The Messners contend, as indicated by the majority opinion, that they are entitled to file a joint federal income tax return for the year 1970 and that Mr. Messner can claim all of the net income for the purpose of securing the ultimate in benefits from the Social Security program; and yet that they may file separate state income tax returns for the avowed purpose of paying less state income tax than would be owing had they filed a joint state income tax return. The tax commissioner has vigorously disputed the Messners' right to file separately. The question is now before this court for decision.

The parties to this action have cited

§§57-38-01.1 and 57-38-31(2), N.D.C.C., and Rule 50(4)b, which was promulgated by the State Tax Commissioner.

Pursuant to §57-38-01.1, N.D.C.C., the North Dakota Legislature has adopted the federal definition of taxable income as the starting point for the computation of state income tax by all taxpayers. This, in essence, results in using the taxable income from Federal Form 1040 as the basis for the North Dakota income tax return. This is true whether a person files a joint return with his spouse or a separate return. Both parties to this action are in agreement on this.

Section 57-38-31(2), N.D.C.C., states that if a person files a joint federal return but wishes to file a separate state return, the taxpayer simply cannot use the taxable income figure which was derived from the federal income tax return by simply dividing such income. He must recalculate his federal taxable income in order to obtain the starting point for the state return. This requires an allocation of income between the spouses based upon certain criteria. Section 57-38-31(2), N.D.C.C., points out the necessary criteria for this determination. It does not set out separate standards for computing taxable income, nor does it relieve the taxpayer from recalculating his federal taxable income.

In the instant case, a careful review of the record fails to show that Mrs. Messner recalculated her taxable income--she merely took one-half of the taxable income from the joint federal return. It must be kept in mind that the evidence which is germane is that evidence covering the year 1970, the income tax year which is in question, and not what may have occurred in other years. The

participation and activity of the taxpayer in the year 1970 is the focal point and the crux of this action. The record is very limited on participation by the taxpayers, particularly of Mrs. Messner, in the year 1970. The primary source of income was from the sale of grain--there was apparently no income from livestock or poultry. The fact that Mrs. Messner may have owned the real estate in joint tenancy with her husband may be one criterion, but it is not decisive. Mere ownership or joint ownership of farm property in itself does not qualify a spouse for self-employment tax purposes (Farmer's Tax Guide - 1971 Edition); nor is joint tenancy ownership in itself sufficient to justify the splitting of income.

Both parties concede that the tax commissioner, pursuant to §57-38-56, N.D.C.C., has the power to promulgate rules and regulations necessary to collect taxes which individuals owe to the State, whether they be income, sales, or use taxes. Rule 50(4)b creates a presumption that, unless expressly shown to the contrary, the spouse claiming all of the income from a joint federal return for self-employment tax purposes, claims that same income for state income tax purposes. The majority opinion further states that the self-serving, unsworn, and unverified declaration of the Messners shows that Mrs. Messner did not consent to her husband's claim of all the joint income for tax purposes. The fact that Mrs. Messner signed the joint federal income tax return belies this contention. By failing to file a self-employment tax return as required by 26 U.S.C. §6017, she has consented to her husband's claim on all the income.

In Woller v. Wisconsin Department of Taxation, 35 Wis. 2d 227, 151 N.W. 2d 170 (1967), the Wisconsin Supreme Court stated

that the burden of showing an error in a tax assessment is on the taxpayer. The Messners concede that the burden is upon them. We adhere to this rule. See generally Evangelical Luth. G. Sam. Soc. v. Board of Cty. Cm'rs, 219 N.W. 2d 900 (N.D. 1974); Y.M.C.A. of N.D. State Univ. v. Board of County Com'rs, 198 N.W. 2d 241 (N.D. 1972). The promulgation of such rules by the tax commissioner, of course, is limited by constitutional restrictions. The application of constitutional prohibitions concerning the collection of taxes has been and still is considered in a distinct category--State ex rel. Haggart v. Nichols, 66 N.D. 355, 265 N.W. 859 (1936), Syll. ¶¶ 5, 6, 7, 8, & 9--as opposed to protection of the constitutional rights of a defendant charged with a crime. Lehnhausen v. Lake Shore Auto Parts Co., 410 U.S. 356, 93 S.Ct. 1001, 35 L.Ed. 2d 351, reh. den. 411 U.S. 910, 93 S.Ct. 1523, 36 L.Ed. 2d 200 (1973).

In the instant case the majority opined that Rule 50(4)b is not unconstitutional per se but is unconstitutional in its application to this case. This court, in Tang v. Ping, 209 N.W. 2d 624 (N.D. 1973), in paragraph 1 of the syllabus, held:

> "A statute that defines adulthood with different ages for males and females, when applied to the Unsatisfied Judgment Fund law, produces an unconstitutional result in that equal protection of the law is denied to males aged eighteen through twenty. . . ."

The factual attention in the Tang case distinguishes it from the case at bar. Likewise, in Boeing Company v. Omdahl, 169 N.W. 2d 696 (N.D. 1969), and in Souris River Telephone Mutual Aid Corp. v. State, 162 N.W. 2d 685 (N.D. 1968), this court upheld the authority

of the tax commissioner with reference to various taxes imposed by the tax commissioner. We accordingly disagree with the majority that there was substantial evidence submitted by the Messners to show that there was in effect an error in the assessment. Again, there is no substantial evidence in the record to show Mrs. Messner's contributions for the 1970 tax year. This court has often held that the decision of administrative agencies will be upheld, provided there is substantial evidence in support of the actions of the various administrative agencies. Soo Line Railroad Company v. City of Wilton, 172 N.W. 2d 74 (N.D. 1969); Application of Northern States Power Co., 171 N.W. 2d 751 (N.D. 1969); George E. Haggart, Inc. v. North Dakota Workmen's Compensation Bureau, 171 N.W. 2d 104 (N.D. 1969); and Williams Electric Cooperative, Inc. v. Montana-Dakota Utilities Co., 79 N.W. 2d 508 (N.D. 1956).

The majority opinion has adopted the view that the self-employment tax is not an integral part of the income tax and, therefore, the filing of a self-employment tax return by Mr. Messner does not bar or estop Mr. and Mrs. Messner from splitting their income and that the tax commissioner was unjustified in treating the Messners' election as conclusive for state income tax purposes. A perusal of §§1401 and 1402 of 26 U.S.C. leads me to a diametrically opposing conclusion, especially in light of the decision of the Fifth Circuit Court of Appeals in Cain v. United States, 211 F. 2d 375, 377, cert. den. 347 U.S. 1013, 74 S.Ct. 868, 98 L.Ed. 1136 (June 7, 1954), in which the Circuit Court stated:

> "What in short is in question here is not the power of congress to lay impost and excises. It is whether congress

> has the power to impose and collect from employees, self or otherwise employed, taxes on the income received from their employment in addition to other income taxes imposed upon them. We see no difficulty in the way of its so doing. Congress can constitutionally, in imposing income taxes, distinguish between earned and unearned income and between income from various kinds of property and occupations, and has often done so. The imposition and collection of an additional income tax on the income of persons not self employed has been going on without contest or question for many years. We think it clear that persons receiving income from self employment can be subjected to additional income taxes on the moneys so received in the same way and to the same extent that persons not self employed can be and are being so subjected."

The Court in Cain 211 F. 2d at 378, supra, again stated:

> "Neither can we find any (warrant) for the view that it (Congress) cannot do what it has done and is doing here, legally impose and legally collect an additional income tax on income derived from self employment, just as it can do, and has long been doing, legally impose and as legally collect an additional income tax from persons otherwise employed."

I believe our court should adhere to this holding.

I also disagree with paragraph 3 of the syllabus in the majority opinion, based on the reasons set forth, supra, in this dissent, because the Messners, by filing a joint federal income tax return and then filing

separate state income tax returns brought themselves within the purview of Rule 50(4)b by their own choice. The majority opinion further does not point out what, if any, individual rights have been abridged by Rule 50(4)b, or that it results in an invidious discrimination to a particular class of persons. I again cite Lehnhausen v. Lake Shore Auto Parts Co., 410 U.S. 356, supra, for its discussion of constitutional prohibition. As previously mentioned, this court has held that a statute is not unconstitutional on the ground that it discriminates against a certain class of people as long as the persons within that class are treated equally. State v. Gamble Skogmo, Inc., 144 N.W. 2d 749 (N.D. 1966); Souris River Telephone Mutual Aid Corp. v. State, 162 N.W. 2d 685 (N.D. 1968); and State ex rel. Haggart v. Nichols, 66 N.D. 355, 265 N.W. 859 (1936). Therefore, adopting the rationale of the above cases, Rule 50(4)b is not unconstitutionally applied by the tax commissioner as evidenced by the facts in the instant case. Furthermore, the Supreme Court of Wisconsin, in Skaar v. Wisconsin Department of Revenue, 211 N.W. 2d 642, 645 (Wis. 1973), quoted with approval from Commissioner of Internal Revenue v. Tower (1946), 327 U.S. 280, 291, 66 S.Ct. 532, 90 L.Ed. 670, in which the United States Supreme Court stated that:

> "'. . . transactions between husband and wife calculated to reduce family taxes should always be subjected to special scrutiny.'"

While I believe that a taxpayer is allowed to avoid paying excess taxes, he should not be allowed to evade taxes that he rightfully owes. In the instant case, the Messners chose to file a joint federal income tax return to maintain maximum social security

APPENDIX B

Bismarck, North Dakota
January 31, 1975

The Supreme Court of the State of North Dakota convened at 3:00 p.m. this 31st day of January, 1975.

Present: The Honorable Ralph J. Erickstad, Chief Justice; the Honorable Wm. L. Paulson, the Honorable Robert Vogel, the Honorable Vernon R. Pederson, the Honorable Paul M. Sand, Associate Justices; Luella Dunn, Clerk.

Now the Court directed the entry of the following order in

FILE #9020

| | |
|---|---|
| Theodore Messner and Margaret Messer, | Petitioners and Appellants |
| v. | |
| Byron L. Dorgan, Tax Commissioner for the State of North Dakota | Respondent and Appellee |

ORDERED, the page i of the syllabus of this case filed on December 31, 1974, be and the same is hereby withdrawn and that page i of the syllabus submitted this day be filed in lieu thereof.

IN THE SUPREME COURT

STATE OF NORTH DAKOTA

| | |
|---|---|
| Theodore Messner and Margaret Messner, | Petitioners and Appellants |
| v. | |
| Byron L. Dorgan, Tax Commissioner for the State of North Dakota, | Respondent and Appellee |

Civil No. 9020

1. Presumption of law arising from Rule 50-4-b of Rules and Regulations of the State Tax Commissioner that person reporting income for Federal self-employment tax purposes claimed all right to such income with the consent of his or her spouse is rebutted by statement of both spouses that no such consent was given and no such claim was made.

2. Where husband and wife file a joint Federal income tax return indicating that all income from their joint enterprise is that of the husband for Federal self-employment tax purposes, State Tax Commissioner may draw an inference from this fact that all income from the joint enterprise is that of the husband.

3. Reviewing court must sustain findings of fact of administrative agency unless such findings are not supported by substantial evidence in light of the entire record.

4. Where, as in this case, findings of fact of administrative agency are not supported by substantial evidence but where evidence in the record is supportive solely of opposing

APPENDIX C

Bismarck, North Dakota
February 5, 1975

The Supreme Court of the State of North Dakota convened at 3:00 p.m. this 5th day of February, 1975.

Present: The Honorable Ralph J. Erickstad, Chief Justice; the Honorable Wm. L. Paulson, the Honorable Robert Vogel, the Honorable Vernon R. Pederson, the Honorable Paul M. Sand, Associate Justices; Luella Dunn, Clerk.

Now the following proceedings were had in

File #9020

| | |
|---|---|
| Theodore Messner and Margaret Messner, | Petitioners and Appellants |
| v. | |
| Byron L. Dorgan, Tax Commissioner for the State of North Dakota | Respondent and Appellee |

It appearing to the Court that an error has been made in the substitute page i of the syllabus presented and filed with the Clerk of the Supreme Court on January 31, 1975;

IT IS ORDERED that substitute page i of the syllabus filed on January 31, 1975 be and the same is hereby withdrawn and that the substitute page i of the syllabus presented and filed this day be substituted in lieu thereof;

IT IS FURTHER ORDERED that under the

provisions of Rule 41 a N.D. R.App.P. the mandate shall issue seven (7) days from this date.

IN THE SUPREME COURT

STATE OF NORTH DAKOTA

Theodore Messner and Margaret Messner, Petitioners and Appellants

v.

Byron L. Dorgan, Tax Commissioner for the State of North Dakota, Respondent and Appellee

CIVIL NO. 9020

1. Presumption of law arising from Rule 50-4-b of Rules and Regulations of the State Tax Commissioner that person reporting income for Federal self-employment tax purposes claimed all right to such income with the consent of his or her spouse is rebutted by statement of both spouses that no such consent was given and no such claim was made.

2. The Federal self-employment tax is a part of the Social Security system and is not a constituent part of the Federal income tax, although self-employment tax returns are filed with personal income tax returns for administrative convenience.

3. A State statute permitting allocation of income between husband and wife cannot be negated by administrative rule which purports to interpret it.

4. It is the duty of the courts to reconcile provisions of law relating to the

same subject matter if possible, and

APPENDIX D-1

STATE OF NORTH DAKOTA IN DISTRICT COURT

COUNTY OF BURLEIGH FOURTH JUDICIAL DISTRICT

Theodore and Margaret Messner, )
)
Appellants, )
)
v. )
)
Byron L. Dorgan, Tax Commissioner )
for the State of North Dakota, )
)
Respondent. )

OPINION OF THE COURT

CIVIL NO. 22284

The above-entitled matter was remanded to the North Dakota State Tax Commissioner for the taking of additional evidence as is required under Sec. 57-38-31(7) on July 3, 1973. To this the taxpayers replied that they had no additional evidence to offer and would stand on the record previously submitted.

It was the position of the Court in the July 3d order that sufficient evidence had not been received to rebut the presumption that all of the income from the jointly owned property is the income of the husband, Theodore Messner, particularly in light of his declaration of taxable income for qualification for federal self-employment purposes. There having been no additional evidence offered or received to rebut the presumption that all the income was that of Theodore

Messner, the matters appealed from are denied and the appeal dismissed.

The appellee will draw an appropriate order dismissing the appeal and present it to the Court for signature.

Dated this 8th day of January 1974.

BY THE COURT:

/s/Alfred A. Thompson
Alfred A. Thompson,
District Judge

APPENDIX D-2

STATE OF NORTH DAKOTA IN DISTRICT COURT

COUNTY OF BURLEIGH FOURTH JUDICIAL DISTRICT

Theodore and Margaret Messner, Appellants,

vs.

Byron L. Dorgan, Tax Commissioner for the State of North Dakota, Respondent.

ORDER FOR JUDGMENT

CIVIL NO. 22284

The above entitled matter having come on before the Court on an Appeal from a Decision of the State Tax Commissioner of North Dakota pursuant to Chapter 57-38 and Chapter 28-32 of the North Dakota Century Code, the matter was submitted to The Honorable Alfred A. Thompson, Judge of the District Court.

The Court, having duly considered the Certificate of Record, the written briefs by counsel for the Appellants and the State Tax Commissioner, the Return to the Remand Order of July 3, 1973, and the other pertinent documents on file herein, determines that the Findings of Fact of the State Tax Commissioner are in accordance with and are supported by the evidence in this matter and further determines that the Conclusions of Law of the State Tax Commissioner are in accordance with

the Findings of Fact and are supported by applicable North Dakota law; and

IT IS HEREBY ORDERED, and the judgment of this Court, that the Decision and Determination as entered by the State Tax Commissioner on November 22, 1972, be hereby in all things affirmed and that the matters appealed from are denied and the Appeal dismissed.

Let Judgment be entered accordingly.

Dated this 17th day of January, 1974, at Bismarck, North Dakota.

BY THE COURT:

/s/ Alfred A. Thompson
Alfred A. Thompson
Judge of the District Court

APPENDIX D-3

STATE OF NORTH DAKOTA IN DISTRICT COURT

COUNTY OF BURLEIGH FOURTH JUDICIAL DISTRICT

Theodore and Margaret Messner, )
)
Appellants, )
)
vs. )
)
Byron L. Dorgan, Tax Commissioner )
for the State of North Dakota, )
)
Respondent. )

JUDGMENT

CIVIL NO. 22284

The Court having considered this matter and having made its Findings of Fact, Conclusions of Law, and having ordered judgment thereon, it is hereby adjudged and determined that the Decision and Determination of the State Tax Commissioner as entered on November 22, 1972, be hereby in all things affirmed and that the matters appealed from are denied and the Appeal dismissed.

Dated this 17th day of January, 1974, at Bismarck, North Dakota.

/s/Thora Dennis
Thora Dennis
Clerk of the District Court

APPENDIX E

STATE OF NORTH DAKOTA IN DISTRICT COURT

COUNTY OF BURLEIGH FOURTH JUDICIAL DISTRICT

Theodore and Margaret Messner,

Appellants,

vs.

Byron L. Dorgan, Tax Commissioner for North Dakota,

Defendant.

TAX COMMISSIONER'S RETURN TO REMAND

ORDER OF DISTRICT COURT

CIVIL NO. 22284

To: Judge Alfred A. Thompson
District Judge
Fourth Judicial District
Burleigh County Courthouse
Bismarck, North Dakota 58501

INTRODUCTION

The above entitled matter was remanded to the North Dakota State Tax Commissioner by you on the 3rd day of July, 1973, for the taking of additional evidence which is required under Section 57-38-31(7) of the North Dakota Century Code and for his finding of the taxpayers having rebutted or failed to rebut the presumption to determine eligibility

for income splitting as is permitted under Section 57-38-31(2) of the North Dakota Century Code.

RESPONSE TO COURT'S INTERPRETATION OF SECTION 57-38-31(7)

In discussing Issue No. 3, as specified by the Court, it is stated on page 7 of the opinion that:

> "Sec. 57-38-31(7) requires that the taxpayer provide to the Tax Commissioner either a true copy of the federal income tax return or equivalent information at any time after he has filed the return required by this chapter if so required by the tax commissioner."

And the Court thereafter continues by stating that:

> "Sec. 57-38-31 authorizes the Tax Commissioner to require information which would support the taxpayer's declaration of income earned."

(Presumably reference is still to Subsection 7 of Section 57-38-31 in the above cited statement.)

In the remand order, as given on page 8, the Court states that:

> ". . . the case is remanded to the North Dakota State Tax Commissioner for the taking of the additional evidence which is required under Sec. 57-38-31(7). . ."

It is this position taken by the Court that the Tax Commissioner questions inasmuch as Section 57-38-31(7) has been construed in two parts by the Tax Commissioner thusly.

The Tax Commissioner has the authority to require that:

I.

(A) A copy of the federal income tax return must accompany the filing of a state income tax return, or

(B) If the taxpayer has no federal copies, equivalent information on other forms furnished by and under regulations promulgated by the Tax Commissioner may accompany the state return when it is filed.

II.

(A) No copy of the federal income tax return need accompany the filing of a state income tax return, but

(B) After the state return is filed, the Tax Commissioner may require that a copy of the federal return be furnished, or

(C) If the taxpayer has no federal copies, equivalent information can be submitted instead.

In administering the tax laws of the state, the Tax Commissioner has exercised option I(A) as set out above and has required that a federal copy must accompany the filing of a state income tax return. This administrative decision and procedure has been conveyed to taxpayers through instructions issued with the income tax forms and through an instruction printed on the form.

In summary, the Tax Commissioner construes Subsection 7 of Section 57-38-31 solely as the granting of authority to him to require copies of federal income tax returns to accompany the filing of state income

tax returns. If the taxpayer has no federal copies, the Tax Commissioner may allow the taxpayer to submit the same information as shown on the taxpayer's original federal income tax return on some other form or in some other manner for state income tax purposes.

ACTION TAKEN ON THE REMAND ORDER

In deference to the order of the Court, issued on the 3rd day of July, 1973, and in compliance therewith the Tax Commissioner acts accordingly:

I.

TAKING OF ADDITIONAL EVIDENCE. Legal Counsel for the office of the State Tax Commissioner did on the 16th day of July, 1973, address correspondence to the attorney for the Plaintiffs-Appellants, wherein it was stated and offered that another formal administrative hearing would be scheduled for the purpose of receiving additional evidence in this case if such a hearing was desired by the Plaintiffs-Appellants.

In response to this stated offer of another administrative hearing, attorney for the Plaintiffs-Appellants did on the 17th day of July, 1973, respond to the office of the State Tax Commissioner and therewith expressed no desire to submit additional evidence and further stated the belief that the present record was adequate.

Copies of the correspondence referred to above were sent to the attention of the Court at that time. Additional copies of this same correspondence are attached to and made a part of this Tax Commissioner's Return to Remand Order of the District Court of the Fourth Judicial District.

II.

ADDITIONAL FINDINGS. The State Tax Commissioner, as hearing officer in this matter, having received the ruling of the Court wherein the case at hand was remanded for purposes of receiving additional evidence and for making additional findings, and having directed correspondence to the attention of the Plaintiffs-Appellants relative to the scheduling of another formal administrative hearing, and having received an answer thereto on behalf of the Plaintiffs-Appellants to the effect that there was no desire to submit any additional evidence and that the present record was considered adequate by the Plaintiffs-Appellants, does hereby take note of these developments and proceedings and in accordance with the further ruling of the Court requesting additional findings hereby makes the following additional findings.

(A) The Plaintiffs-Appellants have stated they have no additional evidence to submit and further state the belief that the present record is adequate.

(B) The Plaintiffs-Appellants have availed themselves of all legal procedural methods as well as having had ample opportunity to present evidence and to be heard in that:

(1) In filing individual income tax returns for the taxable year 1970 they submitted a copy of their joint federal income tax return along with supporting schedules and other information that disclosed how they, the Plaintiffs-Appellants, determined and computed federal taxable income for federal income tax purposes on their 1970 joint federal income tax return.

(2) After receiving a Notice of Assessment of Additional Income Tax and Notice of Protest Procedure from the office of the State Tax Commissioner dated September 1, 1971, Plaintiffs-Appellants filed with the Tax Commissioner a protest, containing objections to assessment on September 27, 1971, wherein the Plaintiffs-Appellants stated the findings to which they took exception and the grounds for their exceptions.

(3) A formal hearing conducted pursuant to the provisions of the Administrative Agencies Practice Act, Chapter 28-32 of the North Dakota Century Code, was held on the 14th day of December, 1971, at the request of the Plaintiffs-Appellants, wherein the Plaintiffs-Appellants did introduce evidence and exhibits and did have the opportunity to be heard. A court reporter was present and a record made of the proceedings. Testimony of the Plaintiffs-Appellants is recorded from page 42 through page 109 of the official transcript of the hearing. Seven exhibits were introduced by the Plaintiffs-Appellants.

(4) An Appeal from the Decision of the Hearing Officer was made to the District Court of the Fourth Judicial District, such Appeal being heard on the 26th day of June, 1973, whereas, with the consent of all parties concerned, the Plaintiffs-Appellants did introduce an additional exhibit into the record and also had the opportunity, with the consent of all parties concerned, to introduce additional evidence.

(5) After the opinion of the Court was issued on the 3rd day of July, 1973, wherein the matter was remanded to the administrative agency for the taking of additional evidence, the Plaintiffs-Appellants elected not to submit any additional evidence and indicated that the existing record was considered adequate.

(6) In attaching a copy of the federal income tax return to the state income tax return of one of the Plaintiffs-Appellants when filed, there was compliance with Section 57-38-31(7) of the North Dakota Century Code, and the information therein requested was submitted in the first instance and no additional request for information pursuant to Section 57-38-31(7) was required.

(C) The Plaintiffs-Appellants have not rebutted the presumption that all of the income from the jointly owned property is the income of the husband, Theodore Messner, one of the Plaintiffs-Appellants.

(1) Section 57-38-31(2) in providing for income from jointly owned property to be allocated between husband and wife according to the capital interest of each, the management and control exercised by each, and the services performed by each with respect to such property or business applies in those situations where neither spouse has claimed all the income as his or her income when filing a federal income tax return for that same income.

(2) The evidence submitted at the administrative hearing indicates that the wife, Margaret Messner, one of the Plaintiffs-Appellants, had some ownership interest of record and that she participated to some degree in the management and control and that she did perform some services, but the evidence submitted does not establish the fact that these activities on her part were engaged in for the purpose of claiming any part of the income from the jointly owned property as her separate income for her income tax purposes.

(3) There has been no express showing, either during the time that the income from the jointly owned property was being earned, or at some point of time after it was earned, that the income was the income of some one other than the husband's, Theodore Messner, and that it was other than his for federal income tax purposes so as to qualify this same income for the husband's self-employment tax purposes.

(D) Plaintiffs-Appellants have not met the requirements of Section 57-38-01.1, Section 57-38-01.2, Section 57-38-31(2) and Rule No. 50(4)(b) in that:

(1) Section 57-38-01.1, enacted later in time than Section 57-38-31(2), takes precedence and expresses the intent of the legislature in that the starting point for the computation of state income tax by all taxpayers shall be federal taxable income.

(2) Section 57-38-01.2, enacted later in time than Section 57-38-31(2), takes precedence and provides that

federal taxable income is the starting point for computing state income taxes.

(3) Section 57-38-31(2), having been superseded, must be interpreted and construed in the light of the legislative intent expressed in Section 57-38-01.1 in that a husband and wife electing to file separate state income tax returns after filing a joint federal income tax return may do so only after they have computed their separate federal taxable income under the provisions of the United States Internal Revenue Code and each then uses this recomputed federal taxable income as the starting point for computing their state income tax.

(4) Section 57-38-31(2), having been superseded, must be interpreted and construed both in conjunction with and subjunctive to Sections 57-38-01.1 and 57-38-01.2 in that when income from jointly owned property is reported for federal income tax purposes as the taxable income of the husband so as to qualify that income for federal self-employment purposes in the husband's name it cannot thereafter be treated in whole or in part as someone else's taxable income for state income tax purposes.

(5) Rule No. 50, and in particular that portion referred to as Rule No. 50(4)(b), was promulgated taking into consideration the filing provisions provided for in Section 57-38-31(2) and the intent of the legislature as expressed in Section 57-38-01.1 and provided for in Section 57-38-01.2.

## CONCLUSION AND DECISION

It is therefore still the decision of the Tax Commissioner that the additional assessment of income taxes on September 1, 1971, in the amount of $290.34 against the Plaintiffs-Appellants, Theodore and Margaret Messner, is correct and is a valid assessment and that the Plaintiffs-Appellants are obligated to pay additional income taxes in that amount to the state.

Dated this 6th day of November, 1973, at Bismarck, North Dakota.

/s/Byron L. Dorgan
Byron L. Dorgan
Tax Commissioner
State of North Dakota

APPENDIX F

STATE OF NORTH DAKOTA IN DISTRICT COURT

COUNTY OF BURLEIGH FOURTH JUDICIAL DISTRICT

| | | |
|---|---|---|
| Theodore and Margaret Messner, Appellants, vs. Byron L. Dorgan, Tax Commissioner for the State of North Dakota, Respondent. | ) | No. 22284 |

## OPINION

This matter comes to the Court on appeal from an administrative ruling rendered by the State Tax Commissioner on November 22, 1972, and on file herein. The facts are essentially not in dispute, and the findings of fact by the Tax Commissioner are adopted by the Court in its opinion.

Counsel for both parties have recited statutes, regulations, opinions and other documents at length in their respective briefs and pleadings, and reference will be made in this opinion to those instruments by identifying titles, document numbers, etc., without setting them out verbatim except where recitation is necessary for interpretation or clarity.

## ISSUES

Contentions between the parties can be narrowed into four separate issues:

1. In view of the discovered and admitted facts, can the taxpayers by law file individual income tax returns?

2. Does the filing of a self-employment tax return by Theodore Messner, showing all income derived from the Messners' joint operations to be solely that of Theodore Messner, prohibit splitting of income on North Dakota income tax returns by filing separate returns?

3. What is the legal interpretation of Rule 50(4)b?

4. Is Rule 50(4)b unconstitutional as an unlawful usurpation of legislative authority?

## ISSUE NO. 1

Statutes, both state and federal, permit the filing of separate income tax returns by husband and wife wherein both have income from properties owned jointly. They may, under N.D.C.C. Sec. 57-38-31(2), include their income in a single joint return; but if they elect to file separate returns, they are required to allocate the income between them in direct proportion to contributions of capital and management. It is clear that under prescribed conditions both the state and federal governments have permitted taxpayers to elect to file either separately or jointly, depending upon the manner in which savings could be best effected. It appears that an election to file separately in one year does not prohibit the parties from filing jointly in any subsequent year, or vice versa. This the appellants have done in the past.

## ISSUE NO. 2

Much of the controversy in this case surrounds the filing by Theodore Messner of

a self-employment tax return, showing all income derived by him in the Messner operation. The question then arises whether that declaration prohibits the Messners from splitting their income on the North Dakota returns as they have sought to do.

The taxpayers contend in their brief that Theodore Messner has, by federal regulation, been required, without choice in the matter, to declare all of the income from the joint operation as his own. Recitation is made of tax conferences wherein it has been suggested by federal authorities that self-employment income should be declared solely on the part of the husband. This is advisory only and not mandatory. The taxpayers' contenion is not sustained by the directive itself, as appears in the Farmer's Tax Guide (Petitioners' Exhibit No. 6, page 42). The controlling language there is as follows:

> "Mere ownership, or joint ownership, of farm property does not qualify a spouse for self-employment tax purposes." (emphasis added)

The regulation clearly establishes that the spouse does not qualify for self-employment tax benefits simply because she is an owner of an interest in properties. However, use of the word "mere" implies that other proofs are available to the spouse, whether male or female, to justify declaration of self-employment earnings. As a matter of fact, Mrs. Messner could have done this had she elected to do so, and she did do so on her state return, evidence further the exhibits and testimony received in the administrative hearing herein. She chose not to provide those proofs to the federal government, electing to give her husband the benefit of his ten years of seniority and the additional earnings in order to improve his social

security benefits in earlier enjoyment thereof.

The question now arises whether this failure to declare self-employment income on her own behalf works an estoppel against her insofar as the State of North Dakota is concerned. To this the answer must be "no." The elements of estoppel are not met insofar as the State of North Dakota either believed the declaration or relied upon it and thereby suffered detriment. Neither was estoppel pleaded especially. But the fact that Mrs. Messner permitted Mr. Messner to declare the entire income as his own income does constitute an admission against interest. The only question remaining is whether this admission against interest is conclusive against her.

It is unfortunate that neither state nor federal returns provide for an identification of the earnings of each of the two joint owners filing on a joint return. The Tax Commissioner takes the position that the only identification as to earnings is that which appears on the Schedule SE (Form 1040) (Court's Exhibit No. 1), wherein the entire earnings are declared to be that of Theodore Messner. The Tax Commissioner now contends that this declaration binds the taxpayer under Rule 50 and prohibits the splitting of income by the two taxpayers on separate returns. Answer to this issue depends upon the answer to Issue No. 3.

ISSUE NO. 3

What is the legal interpretation of Rule 50(4)(b)?

Counsel for the Tax Commissioner have clearly enunciated the purpose of Rule 50(4) b as an employment of an administrative

prerogative authorized by statute, under N.D. C.C. Ch. 57-38. The Tax Commissioner has promulgated and effectuated the rule in accordance with Sec. 28-32-02 by having the rule submitted to the Attorney General for an opinion on legality. Legality was duly determined, but the rule has not, unfortunately been interpreted either by the Attorney General or by the courts of the State of North Dakota, and that is why the issue of interpretation is before the Court here. The language of the rule may require interpretation, but the rule, itself, creates no new authority in the Tax Commissioner not otherwise delegated by statute.

The rule, as well as the statute which it interprets, raises interesting implications insofar as the taxpayers in this situation are involved. For example, I wonder if this case would be before the Court if the age ratio of Mr. and Mrs. Messner were reversed. Would she then have elected to declare all of the income as hers and he none? Interestingly, none of the tax statutes, state or federal, with which we are concerned here take any particular notice of or give any particular respect to the gender of the filing joint owners. Neither should the fact of husband-and-wife relationship create any special right or benefit for either of the declarants under Schedule SE (Form 1040). The issue appears to be that of contribution of capital and effort toward the joint venture. Simply speaking, Petitioners' Exhibit No. 6, the Farmer's Tax Guide, establishes that a spouse acquires no peculiar benefits simply because of ownership, the burden being upon that spouse to establish self-employment benefits by other proofs.

The issue here hinges upon and would appear to rotate solely upon the interpretation of Rule 50(4)b. For purposes of clarity

Rule 50(4)b is hereafter set out in its entirety:

> Allocation of income derived from a business other than a partnership in which both husband and wife claim an ownership interest.
>
> In the case of a business owned by a husband and wife who filed a joint federal income tax return in which one of them claimed all of the income therefrom for federal self-employment tax purposes, it will be presumed for purposes of administering the state income tax law, unless expressly shown to the contrary by the taxpayer, that the spouse who claimed that income for federal self-employment tax purposes did, thereby, with the consent of the other spouse, claim all right to such income and that therefore such income must be included in the state income tax return of the spouse who claimed it for federal self-employment tax purposes if the husband and wife file separate state income tax returns.

There is no question that Rule 50(4)b applies in this case, since the taxpayers are husband and wife who did file a joint federal income tax return in which one of them, Theodore Messner, claimed all of the income for federal self-employment tax purposes. The language of the rule then creates a presumption that the entire income set forth in the federal self-employment tax schedule (Court's Exhibit No. 1) is the income of Theodore Messner for state tax purposes. The rule which establishes the presumption is no paragon of draftsmanship. Therefore, it is necessary to fragment the language in order that some clarity may be derived.

> (I)t will be presumed that . . . the spouse who claimed . . . income for federal self-employment tax purposes did . . . with the consent of the other spouse, claim all right to such income and therefore . . ., etc.

But the intervening language which was extracted from the foregoing is the language which intends and does permit the presumption to be rebutted, and that language is:

> unless expressly shown to the contrary by the taxpayer.

Therefore, even if Theodore Messner declared all of the income as his income for self-employment tax purposes, thereby raising a presumption that all of the income was his income, Margaret Messner is in a position to show to the contrary that it was not entirely his income, thereby permitting a splitting of income on separate state income tax returns.

The question now arises whether Margaret Messner did, in fact, sustain the burden of rebutting the presumption which was raised, by providing to the Tax Commissioner that information which would establish her right to file a separate income tax return under Sec. 57-38-31(2). The language of the second paragraph thereof becomes extremely important, and particularly this much thereof;

> A husband and wife who have income from property or business in which both have an ownership interest . . . may file separate returns in the same way as provided in the preceding paragraph, provided that the property or business in which both have an ownership interest shall be allocated between them according

> to the capital interest of each, the management and control exercised by each, and the services performed by each with respect to such property or business, pursuant to rules and regulations promulgated by the tax commissioner for the reasonable allocation thereof.

Rule 50(4)b is one of such rules.

The taxpayer declarations accompanying the income tax return do not satisfy the requirements of this provision. They are simply self-serving declarations and not proof. Sec. 57-38-31(7) requires that the taxpayer provide to the Tax Commissioner either a true copy of the federal income tax return or equivalent information.

> at any time after he has filed the return required by this chapter if so required by the tax commissioner. (emphasis added)

Sec. 57-38-31 authorizes the Tax Commissioner to require information which would support the taxpayer's declaration of income earned. Income Tax Rule 50(4)b further authorizes the taxpayer to rebut a presumption that all taxable income belongs to the declarant under Schedule SE (Form 1040) (Court's Exhibit No. 1). The Court finds, therefore, that the declaration of self-employment income is not conclusive upon the declarant or his spouse unless he is unable to rebut the presumption by presentation of other evidence to the Tax Commissioner as permitted under Sec. 57-38-31 (2) and the promulgated Rule 50(4)b.

The decision of the Tax Commissioner makes no mention of the proof which has heretofore been provided by the taxpayers

to support their contentions of equivalent ownership, management, control, and services provided by each. The record does not disclose that the Tax Commissioner has ever required of the taxpayers that they provide that information as is permitted under Sec. 57-38-31(7). Petitioners' Exhibits A, B, C, and D tend to provide some proof of ownership of assets, and testimony taken of Mr. and Mrs. Messner in the administrative hearing provide some insight into ownership, management, control, and services provided by the two of them. However, absent the showing that the Tax Commissioner has required additional information to be filed in support of the taxpayers' declarations and no finding ever having been made that the information required under Sec. 57-38-31(7) is insufficient to support the declarations, the Court finds that the question has not been administratively resolved.

In light of the foregoing, the case is remanded to the North Dakota State Tax Commissioner for the taking of the additional evidence which is required under Sec. 57-38-31(7) and for his finding of the taxpayer's having rebutted or failed to rebut the presumption to determine eligibility for income splitting as is permitted under Sec. 57-38-31(2).

ISSUE NO. 4

The Court has not really reached the question of the unconstitutionality of Rule 50(4)b as an unlawful usurpation of legislative authority. But a comment might be helpful. If Rule 50(4)b had limited the taxpayer to the declaration made by her spouse of self-employment income under Court's Exhibit No. 1 (Schedule SE [Form 1040[), the

rule would without question be void as an unlawful usurpation of legislative authority, simply because the rule limits broader rights granted the taxpayer under Chapter 57-38. But the rule does not go that far and may be helpful as an interpretation of the statute. It might be added, in passing, the rule lends little to the statute by way of clarification and, as a matter of fact, needs clarification itself if it is to serve any legitimate purpose.

Dated this 3d day of July 1973.

BY THE COURT:

/s/Alfred A. Thompson
Alfred A. Thompson
District Judge

APPENDIX G

STATE OF NORTH DAKOTA BEFORE THE TAX COMMISSIONER

COUNTY OF BURLEIGH OF THE STATE OF NORTH DAKOTA

BISMARCK, NORTH DAKOTA

In the Matter of the Income )
Tax Determination Made by the )
State Tax Commissioner Against)
Theodore and Margaret Messner,)
Sanborn, North Dakota. )

FINDINGS OF FACTS, CONCLUSIONS OF LAW AND DECISION OF THE TAX COMMISSIONER OF THE STATE OF NORTH DAKOTA

The above entitled matter came on for hearing before John W. Frith, Hearing Officer, designated by the Tax Commissioner of the State of North Dakota, to hear the matter in the State Capitol, Bismarck, North Dakota, at 1:30 p.m., December 14, 1971, which hearing was held pursuant to the provisions of the Administrative Agencies Practice Act, Chapter 28-32 of the North Dakota Century Code, as provided for in Section 57-38-39 of the North Dakota Century Code.

Theodore and Margaret Messner, the taxpayers, and hereinafter referred to as "petitioners", were represented by their attorney, L. A. W. Stephan, Valley City, North Dakota, and the Tax Commissioner of the State of North Dakota, hereinafter referred to as "Tax Commissioner", was represented by Albert R. Hausauer and Robert W. Wirtz, Special Assistant Attorney Generals for the office of the State Tax Commissioner.

Seven exhibits were offered by the Petitioners and received in evidence and the testimony of three witnesses called by the attorney for the Petitioners was taken.

Four exhibits were offered by the Tax Commissioner and received in evidence and the testimony of two witnesses called by the attorneys for the Tax Commissioner was taken.

Upon consideration of the exhibits, testimoney, briefs filed by the attorneys for the Petitioners and for the Tax Commissioner, and other documents that are a part of the record of this proceeding, the Tax Commissioner makes the following Findings of Facts, Conclusions of Law and Decision.

## FINDINGS OF FACTS

I.

The Petitioners, Theodore and Margaret Messner, are husband and wife and have been married since 1935. Their post office address is Sanborn, North Dakota 58480, and they reside on a farm in Anderson Township, Barnes County. The farm unit consisting of 800 acres was acquired by the purchase of 160 acres in 1941 by Theodore Messner, one of the Petitioners, from John E. Strong, and by purchase of 640 acres by contract for deed in 1956, by Theodore and Margaret Messner, the Petitioners, from Mary Messner. As to the 160 acres purchased in 1941 by Theodore Messner, one of the Petitioners, title was recorded in 1941, and subsequently title to this property was transferred to the joint names of the Petitioners, Theodore and Margaret Messner, in 1969, and this title was so recorded in 1969. As to the 640 acres purchased by Petitioners under a contract of deed signed in 1956, title was recorded in 1967 in the joint names of the Petitioners.

II.

The Petitioners have lived on the farm unit since their marriage in 1935, renting the farm unit until the purchase dates set out in paragraph I, above. Starting in 1935, both of the Petitioners shared in the work required in operating the farm unit and providing for and raising five children. During this period of time, from 1935 through 1970, Margaret Messner, one of the Petitioners, performed services, including milking, raising chickens, feeding and watering livestock, keeping farm records, paying bills, cooking for hired hands, accompanying her husband, one of the Petitioners, to the County ASC and other governmental offices regarding government programs and participating in the discussion therein, accompanying her husband, one of the Petitioners, to the offices of their tax advisor and participating in the discussion regarding the preparation of state and federal income tax returns, and discussing with her husband, one of the Petitioners, the management of the farm unit. One of the children of the Petitioners, Donald, age 34, lives at home with the Petitioners and farms land he rents from others and assists the Petitioners in operating the Petitioners' farm unit.

III.

For the calendar years 1963, 1964, 1965, 1966, 1967 and 1969, the Petitioners filed joint state income tax returns. For the calendar years 1968 and 1970 the Petitioners filed separate individual state income tax returns.

IV.

On March 31, 1971, Theodore Messner, one of the Petitioners, filed with the office of

the State Tax Commissioner, North Dakota individual income tax return, Form 37, for the calendar year 1970, bearing the signature of Theodore Messner. Entered and reported on line 1, in Schedule 2, on page 2 of this return was $6,740.90 which is 50% of the adjusted gross income as shown on line 18 of the copy of the joint federal income tax return, Form 1040, which was attached to the Petitioner's Form 37. North Dakota state income tax in the amount of $70.08 computed on a North Dakota taxable income of $4,669.46 was paid when the return was filed. Attached to the state income tax return of Theodore Messner, one of the Petitioners, was a statement signed by both the Petitioners entitled, "STATEMENT OF HUSBAND AND WIFE RELATIVE TO INCOME FROM FARMLAND HELD IN JOINT TENANCY OWNERSHIP."

V.

On March 31, 1971, Margaret Messner, one of the Petitioners, filed with the office of the State Tax Commissioner, North Dakota individual income tax return, Form 37, for the calendar year 1970, bearing the signature of Margaret Messner. Entered and reported on line 1, in Schedule 2, on page 2 of this return was $6,740.90, which is 50% of the adjusted gross income as shown on line 18 of the copy of the joint federal income tax return, Form 1040, which was attached to the state return, Form 37, of Theodore Messner, one of the Petitioners. North Dakota state income tax in the amount of $83.47, computed on a North Dakota taxable income of $5,269.46 was paid when the return was filed. Attached to the state income tax return of Margaret Messner, one of the Petitioners, was a statement signed by both Petitioners entitled, "STATEMENT OF HUSBAND AND WIFE RELATIVE TO INCOME FROM FARMLAND HELD IN JOINT TENANCY OWNERSHIP."

VI.

Theodore and Margaret Messner, the Petitioners, filed a joint federal income tax return for the calendar year 1970 with the federal government and a copy of this 1970 federal income tax return was attached to the state income tax return of Theodore Messner, one of the Petitioners. The copy of the 1970 federal income tax return consists of pages 1 and 2 of Form 1040, Schedules A and B of Form 1040, a farm schedule for 1970 for Theodore and Margaret Messner, and a depreciation schedule for 1970 for Theodore Messner. The total federal tax liability as shown on this copy of Form 1040, on page 1, line 25, amounts to $2,540.70, and is a total of the income tax computation of $1,953.50 on a federal taxable income of $10,606.80, the tax surcharge computation of $49.00 on a federal income tax liability of $1,953.50, and the self-employment tax computation of $538.20 on self-employment income of $7,800.00.

VII.

In the joint income tax return filed by the Petitioners for 1970 federal income tax purposes, all the net income from the operations of the farm unit was treated as the income of Theodore Messner, one of the Petitioners, qualifying him for federal self-employment tax purposes, and this self-employment tax was paid by Theodore Messner on the maximum amount of income permissable, which was $7,800.00.

VIII.

On September 1, 1971, the State Tax Commissioner assessed additional income tax on the 1970 state income tax returns of Theodore and Margaret Messner, the Petitioners, in the amount of $290.34, and a Notice of Determination and Assessment was mailed to the

Petitioners.

Computation of the additional income tax assessment consisted of starting with the adjusted gross income figure of $13,481.80 as shown on the copy of the federal income tax return submitted with Theodore Messner's, one of the Petitioners, separate individual North Dakota state income tax return, and deducting therefrom a standard deduction of $1,000.00, personal exemptions of $1,800.00, an additional personal exemption for filing a joint North Dakota state income tax return of $300.00, and a federal income tax deduction of $742.88. The result was a North Dakota taxable income figure of $9,638.92 which resulted in a North Dakota income tax computation figure of $443.89. From this tax computation figure was deducted the North Dakota state income tax each of the Petitioners had paid on their 1970 separate individual North Dakota state income tax returns which had been previously filed, being a combined total of $153.55, and leaving a balance due of $290.34, which is the amount of the additional income tax assessment.

IX.

On September 27, 1971, the Tax Commissioner received "Objections to Assessment" on behalf of the Petitioners and a reconsideration and redetermination were requested. On November 1, 1971, the Petitioners requested a formal hearing.

X.

Section 57-38-01.1 of the North Dakota Century Code provides in part as follows:

> "57-38-01.1. DECLARATION OF LEGISLATIVE INTENT.--It is the intent of the legislative assembly to simplify the

state income tax laws and to demonsrate that federal legislation is not necessary to deal with certain interstate tax problems, by adopting the federal definition of taxable income as the starting point for the computation of state income tax by all taxpayers and providing the necessary adjustments thereto to substantially preserve and maintain existing exemptions and deductions."

XI.

Section 57-38-01.2 of the North Dakota Century Code provides in part as follows:

"57-38-01.2. ADJUSTMENTS TO TAXABLE INCOME FOR INDIVIDUALS AND FIDUCIARIES. --1. The taxable income of an individual, estate or trust as computed pursuant to the provisions of the United States Internal Revenue Code of 1954, as amended, shall be:"

XII.

Section 57-38-31(2) of the North Dakota Century Code provides in part as follows:

"2. A husband and wife each having separate income may include their income in a single joint return, or if they have separate income from personal or professional services or from business or property in which the other has no ownership and if they file a joint federal income tax return in which such income is reported, they may file separate returns in which the separate income of each and the deductions and exemptions for themselves or their dependents are reported in the same way that they would have been required to report them in separate federal returns if they had

filed separate federal returns.

"A husband and wife who have income from property or business in which both have an ownership interest may file a single joint return in which the income of both, along with any other income they may be required to report, is included, or they may file separate returns in the same way as provided in the preceding paragraph, provided that the income from the property or business in which both have an ownership interest shall be allocated between them according to the capital interest of each, the management and control exercised by each, and the services performed by each with respect to such property or business, pursuant to rules and regulations promulgated by the tax commissioner for the reasonable allocation thereof."

XIII.

Income Tax Rule No. 50 as promulgated by the State Tax Commissioner and as approved by the Attorney General on April 24, 1970, provides in part as follows:

"INCOME TAX RULE NO. 50

REPORTING OF INCOME BY HUSBAND AND WIFE

"A husband and wife who have separate income and who have elected to file a joint federal income tax return are permitted, pursuant to subsection 2 of section 57-38-31 of the North Dakota Century Code, to file separate North Dakota income tax returns. The election by spouses to report income separately for North Dakota income tax purposes is subject to the condition that such income

is correctly allocated between husband and wife and reported in the same manner as they would have been required to report such income in separate federal returns. Thus, where a husband and wife determine their federal income tax for a particular year on a joint return and elect to determine their North Dakota income taxes separately, they are required to compute their North Dakota adjusted gross incomes separately; that is, in the same manner as if the federal adjusted gross income of each spouse had been determined on separate federal returns filed by them.

"The provisions of this rule shall be applicable to income tax returns that have been or will be filed pursuant to subsection 2 of section 57-38-31 of the North Dakota Century Code."

## CONCLUSIONS OF LAW

I.

A husband and wife may file separate individual North Dakota state income tax returns in which the separate income of each and the deductions and exemptions for themselves or their dependents are reported in the same way that they would have been required to report them in separate federal returns if they had filed separate federal returns.

II.

The starting point for the computation of state income tax by all taxpayers is taxable income as computed pursuant to the provisions of the United States Internal Revenue Code of 1954, as amended.

III.

A husband and wife in filing a joint federal income tax return wherein the income from jointly owned property is considered the income of the husband so as to qualify the husband for self-employment tax coverage and then report this income as the husband's self-employment income for self-employment tax computation, cannot thereafter claim this same income to be other than the husband's when filing state income tax returns.

IV.

Income Tax Rule No. 50 is not legislative nor arbitrary but is a reasonable interpretation of the applicable provisions of law and only prescribes the method and procedure required under Chapter 57-38 of the North Dakota Century Code for the filing of separate income tax returns by a husband and wife.

V.

The Tax Commissioner's assessment of additional income tax on September 1, 1971, against the Petitioners in the amount of $290.34 for the year 1970 is a correct and valid assessment.

DECISION

A decision of this matter involves the interpretation of Section 57-38-01.1, Section 57-38-01.2, Section 57-38-31(2) and the application of Income Tax Rule No. 50, as well as the opinions of the Attorney General as issued over the years.

The administrative hearing brief of the State Tax Commissioner as submitted to the Hearing Officer prior to the hearing, reviewed the laws and procedures as they pertain to this

matter. The review includes a historical summary of the statutes affecting the subject matter of this hearing and the Attorney General's opinions bearing directly on the subject matter. Further, this review brings out the fact that the Tax Commissioner included in the instructions for the 1970 income tax return a statement pertaining to the filing of income tax returns by married taxpayers who filed joint federal income tax returns and who desired to file separate North Dakota state income tax returns, and this instruction stated that additional information on the subject was available from the Tax Department offices upon request.

Included in this additional information would be Income Tax Rule No. 50, promulgated by the office of the State Tax Commissioner and approved by the Attorney General on April 24, 1970.

Section 57-38-31(2) of the North Dakota Century Code, as amended by the 1967 legislature, provides that a husband and wife who have income from property or business in which both have an ownership interest may file separate state income tax returns in which the separate income of each and the deductions and exemptions for themselves, or their dependents, are reported in the same way that they would have been required to report them in separate federal income tax returns had they filed separate federal income tax returns.

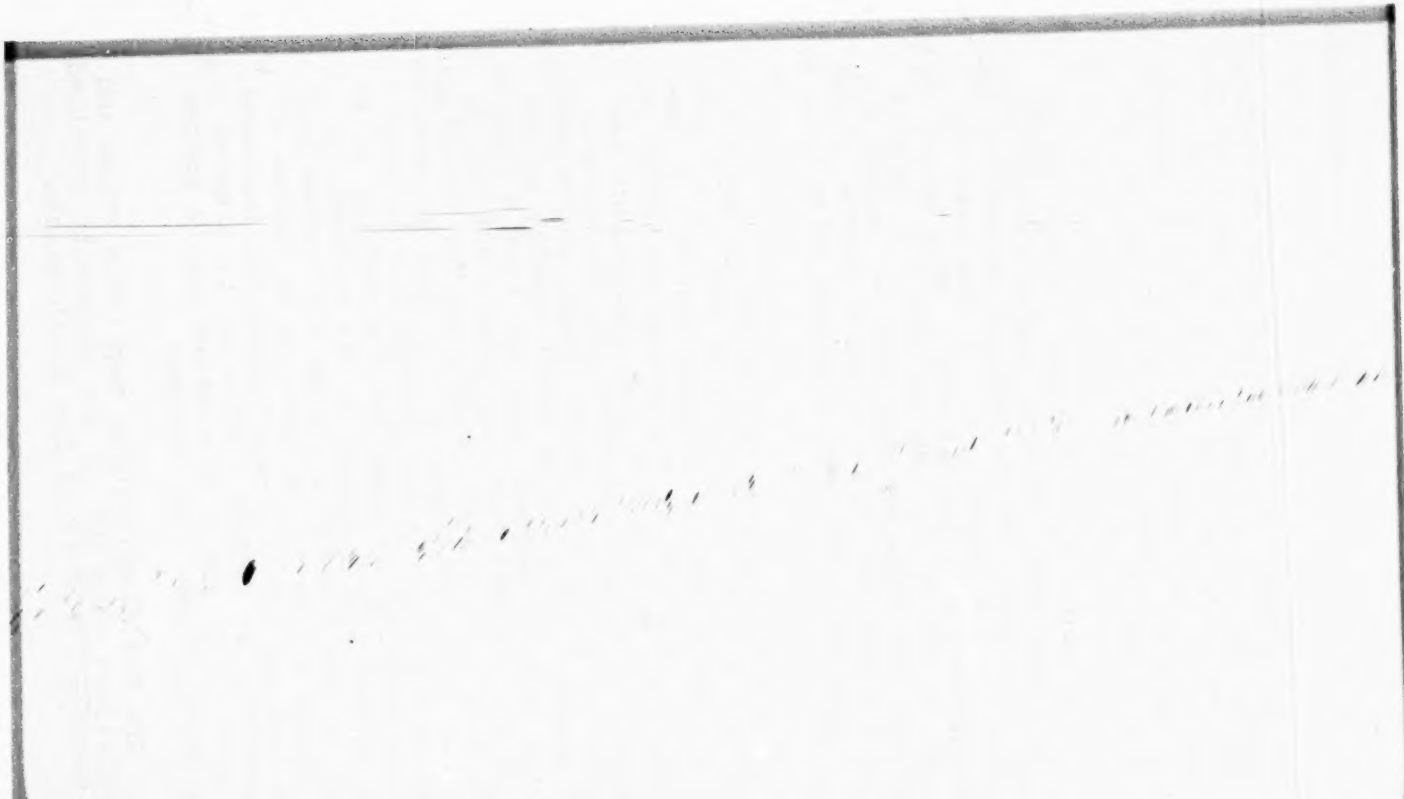
And how separate state income tax returns would have to be filed to conform with the way that separate federal income tax returns are filed is set out in Section 57-38-01.1 and Section 57-38-01.2 of the North Dakota Century Code. In these sections the 1967 legislature spelled out its intent and provided that the federal taxable

income arrived at in preparing one's federal income tax return would be the starting figure that must be used in computing North Dakota state income tax, subject to certain adjustments, none of which pertain to the subject matter at hand.

In arriving at federal taxable income when preparing a federal income tax return, the provisions of the federal income tax law pertaining to what is income and what are deductions must be followed. This means that what is income for the husband for federal income tax purposes must also be income for the husband for state of North Dakota income tax purposes, the same standard being true as to the wife.

Income Tax Rule No. 50 recognizes the federal income tax provision that there can be no assignment of income; that the income must be reported by the person who earns it. Income Tax Rule No. 50 also recognizes the general principle to which the Petitioners refer, that jointly owned income and property of husband and wife is owned equally by the joint owners, and one does not have a greater interest therein than the other; but Income Tax Rule No. 50 also recognizes the exceptions to the above principle and it does so when it recognizes that if the income from jointly owned property is reported for federal self-employment tax purposes by the husband, it must be the husband's income for income tax purposes before it can qualify as income of the husband for self-employment tax purposes. Therefore, it cannot thereafter be treated in part or in whole as someone else's income for state income tax purposes.

The Tax Commissioner may issue rules and regulations pursuant to the authority provided in Section 57-38-56 of the North Dakota



Century Code, and furthermore, the closing sentence of Section 57-38-31(2) of the North Dakota Century Code, expressly authorizes the Tax Commissioner to issue rules and regulations pertaining to the filing of income tax returns by married taxpayers. Income Tax Rule No. 50 is within this authority and is necessary for the practical administration of the income tax statutes and is not legislative nor unconstitutional in its application.

The Petitioners in their testimony have brought out that Margaret Messner has performed services and has participated in the farm unit operation over the past thirty-five years, and that the title to the farm unit property is in the names of both Petitioners. But there has been no showing that Margaret Messner ever considered any of the income as her separate income. Exactly the opposite is true, the income has always been considered the income of the husband for income tax purposes and therefore self-employment tax purposes. As we are concerned only with the 1970 state income tax return, the law as it applies to the 1970 return is the law that must be considered. Therefore, the statutes as they read since last being amended by the legislature are controlling, and the sections under consideration were last amended in 1967.

It is therefore the decision of the Tax Commissioner that the additional assessment of income taxes on September 1, 1971, in the amount of $290.34 against the Petitioners, Theodore and Margaret Messner, is correct and is a valid assessment and that the Petitioners are obligated to pay additional income taxes in that amount to the state.

Dated this 22nd day of November, 1972 at Bismarck, North Dakota.

/s/Byron L. Dorgan

Byron L. Dorgan
Tax Commissioner
State of North Dakota

## APPENDIX H

### STATEMENT OF HUSBAND AND WIFE RELATIVE TO INCOME FROM FARMLAND HELD IN JOINT TENANCY OWNERSHIP

Taxpayers, husband and wife, have filed a joint federal income tax return for 1970 listing joint income from farmland held in joint tenancy ownership. Under federal regulations (see below*) husband was required to pay self-employment tax on all earnings from farm. Wife was not permitted to claim part for self-employment tax purposes. This was not optional on the part of either.

This statement is made to set forth clearly that taxpayers on their separate state income tax returns each claims his share of income from jointly owned land, that neither has given any consent of any kind to husband's including such income in the federal tax return for self-employment purposes, and that such was done because it was mandatory under federal laws and regulations.

Dated 3/26/71.

/s/Margaret Messner
/s/Theodore Messner

*Farmers' Tax Guide - 1971 Edition. "Your wife is not considered 'selfemployed' with respect to your earnings from self-employment, even though you file a joint income tax return . . . mere ownership or joint ownership, of farm property does not qualify a spouse for self-employment purposes."

## APPENDIX I

STATE OF NORTH DAKOTA STATUTORY PROVISIONS OF THE NORTH DAKOTA CENTURY CODE REPRODUCED TO SUPPORT THE PETITION FOR CERTIORARI, ALONG WITH EXCERPTS FROM RULES AND REGULATIONS PROMULGATED IN REFERENCE TO AND FURTHERANCE THEREOF

Section 57-38-31(2) of the North Dakota Century Code is quoted as follows:

"2. A husband and wife each having separate income may include their income in a single joint return, or if they have separate income from personal or professional services or from business or property in which the other has no ownership and if they file a joint federal income tax return in which such income is reported, they may file separate returns in which the separate income of each and the deductions and exemptions for themselves or their dependents are reported in the same way that they would have been required to report them in separate federal returns if they had filed separate federal returns.

"A husband and wife who have income from property or business in which both have an ownership interest may file a single joint return in which the income of both, along with any other income they may be required to report, is included, or they may file separate returns in the same way as provided in the preceding paragraph, provided that the income from the property or business in which both have an ownership interest shall be allocated between them according to the capital interest of each, the management and control exercised by each, and the services performed by each with respect to such property or business, pursuant to rules and regulations promulgated by the tax commissioner for the reasonable allocation thereof."

Section 57-38-01.1 of the North Dakota Century Code is quoted as follows:

"57-38-01.1. DECLARATION OF LEGISLATIVE INTENT.--It is the intent of the legislative assembly to simplify the state income tax laws and to demonstrate that federal legislation is not necessary to deal with certain

interstate tax problems, by adopting the federal definition of taxable income as the starting point for the computation of state income tax by all taxpayers and providing the necessary adjustments thereto to substantially preserve and maintain existing exemptions and deductions.

"It is the further intent of the legislative assembly to eliminate double taxation of the earnings of small corporations by recognizing a subchapter S election when made for federal income tax purposes."

Rule 57-38-050:

"RULE NO. 57-38-050 REPORTING OF INCOME BY HUSBAND AND WIFE

"A husband and wife who have separate income and who have elected to file a joint federal income tax return are permitted, pursuant to subsection 2 of section 57-38-31 of the North Dakota Century Code, to file separate North Dakota income tax returns. The election by spouses to report income separately for North Dakota income tax purposes is subject to the condition that such income is correctly allocated between husband and wife and reported in the same manner as they would have been required to report such income in separate federal returns. Thus, where a husband and wife determine their federal income tax for a particular year on a joint return and elect to determine their North Dakota income taxes separately, they are required to compute their North Dakota adjusted gross incomes separately; that is, in the same manner as if the federal adjusted gross income of each spouse had been determined on separate federal returns filed by them.

"The provisions of this rule shall be applicable to income tax returns that have been or will be filed pursuant to subsection 2 of section 57-38-31 of the North Dakota Century Code.

"Requirements for several of the various special situations arising from these different methods of filing a return under the federal and state income tax laws are set out below.

. . . .

"4. INCOME FROM A BUSINESS IN WHICH BOTH HUSBAND AND WIFE HAVE AN OWNERSHIP INTEREST:

"Income derived from a business the ownership of which is in both spouses, as evidenced by record title or by the existence of a bona fide partnership agreement or by other recognized method of establishing legal ownership, may be allocated between spouses and reported on separate individual state income tax returns provided that the interest of each spouse is allocated according to the capital interest of each, the management and control exercised by each, and the services performed by each with respect to such business. Compliance with the conditions contained in subparagraphs a or b of this paragraph and consideration of subparagraphs c, d and e of this paragraph must be made in allocating income from a business in which both husband and wife have an ownership interest.

. . . .

"b. ALLOCATION OF INCOME DERIVED FROM A BUSINESS OTHER THAN A PARTNERSHIP IN WHICH BOTH HUSBAND AND WIFE CLAIM AN OWNERSHIP INTEREST

"In the case of a business owned by a husband and wife who filed a joint federal income tax return in which one of them claimed all of the income therefrom for federal self-employment tax purposes, it will be presumed for purposes of administering the state income tax law, unless expressly shown to the contrary by the taxpayer, that the spouse who claimed that income for federal self-employment tax purposes did, thereby, with the consent of the other spouse, claim all right to such income and that therefore such income must be included in the state income tax return of the spouse who claimed it for federal self-employment tax purposes if the husband and wife file separate state income tax returns."

## APPENDIX J

FEDERAL STATUTES, ORDERS AND REGULATIONS:

26 USC 1401(a) Old age, survivors, and disability insurance.-In addition to other taxes, there shall be imposed for each taxable year, on the self-employment income of every individual, a tax as follows: . . .

26 USC 1402(a) Net earnings from self-employment.-The term "net earnings from self-employment" means the gross income derived by an individual from any trade or business carried on by such indivual, less the deduction allowed by this subtitle which are attributable to such trade or business, plus his distributive share (whether or not distributed) of income or loss described in Section 702(a)(9) from any trade or business carried on by a partnership of which he is a member; except that in computing such gross income and deductions and such distributive share of partnership ordinary income or loss -

(5) if

(A) any of the income derived from a trade or business (other than a trade or business carried on by a partnership) is community income under community property laws applicable to such income, all of the gross income and deductions attributable to such trade or business shall be treated as the gross income and deductions of the husband unless the wife exercises substantially all of the management and control of such trade or business,

in which case all of such gross income and deductions shall be treated as the gross income and deductions of the wife; and

26 USC 1402(b) Self-employment income.-The term "self-employment" means the net earnings from self-employment derived by an individual (other than a nonresident alien individual)during any taxable year . . . .

26 USC 1402(c) Trade or business.-The term "trade or business", when used with reference to self-employment income or net earnings from self-employment, shall have the same meaning as when used in section 162 (relating to trade or business expenses), . . . .

26 USC 6012 Persons required to make returns of income

(a) General rule. Returns with respect to income taxes under subtitle A shall be made by the following:

(1) Every individual having for the taxable year a gross income of $600 or more . . . .

26 USC 6017 Self-employment tax returns.- Every individual (other than a nonresident alien individual) having net earnings from self-employment of $400 or more for the taxable year shall make a return with respect to the self-employment tax imposed by chapter 2. In the case of a husband and wife filing a joint return under section 6013, the tax imposed by chapter 2 shall not be computed on the aggregate income but shall be the sum

of the taxes computed under such chapter on the separate self-employment income of each spouse.

# In the
# Supreme Court of the United States

MICHAEL RODAK, JR., CLERK

OCTOBER TERM, 1974

No. 74-1225

BYRON L. DORGAN, NORTH DAKOTA
STATE TAX COMMISSIONER,

*Petitioner*

vs.

THEODORE MESSNER and
MARGARET MESSNER,

*Respondents*

On Petition for a Writ of Certiorari
to the Supreme Court of North Dakota

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## REPLY OF PETITIONER TO RESPONDENTS' LETTER IN OPPOSITION TO PETITION

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*Counsel for Petitioner*

IN THE
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1974

NO. 74-1225

Byron L. Dorgan, North Dakota
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vs.

Theodore Messner and
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Respondents.

ON PETITION FOR A WRIT OF CERTIORARI
TO THE SUPREME COURT OF NORTH DAKOTA

# REPLY OF PETITIONER TO RESPONDENTS' LETTER IN OPPOSITION TO PETITION

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Counsel for Petitioner

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ON PETITION FOR A WRIT OF CERTIORARI
TO THE SUPREME COURT OF NORTH DAKOTA

REPLY OF PETITIONER TO RESPONDENTS'
LETTER IN OPPOSITION TO PETITION

The purpose of this reply is to refute the statements made by the Respondents in their letter of April 8, 1975, addressed to this Court, wherein it was stated that they were waiving their right to file a reply brief in opposition to the Petition for a Writ of Certiorari to the Supreme Court of North Dakota.

However, in this letter of April 8, 1975, the Respondents made the statement that no federal question of substance had been decided by the Supreme Court of North Dakota and that no federal question of substance was involved or decided. Other contentions were also advanced.

Therefore, the Respondents' letter of April 8, 1975, should be considered as a reply brief even though it may not be in strict compliance with the rules and procedures of this Court, thus entitling the Petitioner to reply to the statements and contentions advanced therein.

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## CITATIONS

The provisions of the federal and state statutes cited below are reproduced in the separate Appendix filed with the Petition for a Writ of Certiorari to the Supreme Court of North Dakota in the instant matter.

FEDERAL STATUTES:

26 USC 1401
26 USC 1402(b)
26 USC 1402(a)(5)(A)
26 USC 6012
26 USC 6017

NORTH DAKOTA STATUTES:

57-38-01.1 NDCC
57-38-31(2) NDCC

## REPLY ISSUES INVOLVED

1. Was a federal question of substance involved or decided by the Supreme Court of North Dakota? We submit that there was.

2. Does this Court have jurisdiction to review the judgment of the Supreme Court of North Dakota? We submit that it does.

## STATEMENT

The Respondents in their letter of April 8, 1975, take the position that no federal question of substance was involved or decided by the Supreme Court of North Dakota. The Respondents position being that the questions presented in the lower courts involved only state statutes and the interpretation of an administrative rule of the North Dakota State Tax Commissioner.

The above stated position of the Respondents is not supported by the record in the courts below, the administrative hearing, the appeal to the State District Court and the appeal to the North Dakota Supreme Court. The Respondents in this Court were the Petitioners in the Courts below and it is interesting to note that the Respondents in this Court were always ready, willing and financially able to pursue the issues involved until a ruling in their favor was achieved, a ruling that did not properly address itself to the issues and the federal questions presented.

## ARGUMENT

The issues in this case are not solely the issues of state law. Because of the federalizing of the state income tax law (Section 57-38-01.1 NDCC) the provisions of Section 57-38-31(2) NDCC call for the interpretation of federal statutes.

Section 57-38-31(2) NDCC in essence provides that a husband and wife who have income from property or business in which both have an ownership interest may file separate state income tax returns provided the separate income of each is reported in the same way the income would have been required to be reported in separate federal returns. The interpretation of federal statutes is thus required and a substantial federal question is presented.

The Supreme Court of North Dakota did not properly address itself to the issues involved and the federal questions involved. The lower court did not recognize that because of "federalizing" the reporting of income by a husband and wife on separate state income tax returns had to follow the federal statutes and regulations governing the filing of separate federal income tax returns. That is, each taxpayer must report his or her own separate income and that no option existed under federal law that permitted the reporting of income one way for income tax purposes and another way for self-employment tax purposes.

Instead, the Supreme Court of North Dakota determined that the self-employment tax was not a part of the federal income tax, but rather, that it was a separate tax, the return of which was filed with the federal income tax return for administrative convenience only. The Supreme Court of North Dakota

based this belief on its interpretation of the provisions of 26 USC 1401 and 1402(b), imposing the tax and defining net earnings from self-employment, and 26 USC 6017, imposing a duty to file a self-employment tax return, irrespective of whether an income tax return was required under 26 USC 6012.

The Supreme Court of North Dakota misinterpreted federal statutes when it ruled that a taxpayer had the option to claim all the income from property jointly owned with his wife as his self-employment income and that this had no bearing upon his, or her, income tax liability, state or federal, and did not justify the Tax Commissioner treating that election as conclusive for state income tax purposes. Under this interpretation, that the self-employment tax is a separate federal tax, and not a part of the federal income tax, spouses who jointly own property (in non-community property states) may elect to report the joint income from that property jointly for federal income tax purposes and separately as to one spouse for self-employment tax purposes.

The Supreme Court of North Dakota observed that the Federal Internal Revenue Code made provision for a husband to claim all the income in a community property state for self-employment tax purposes, regardless of the fact that the income was equally divided for income tax purposes. (26 USC 1402 (a)(5)(A)) However, the Internal Revenue Code makes no provision whatsoever for the resolution of a similar question arising in a state, such as North Dakota, that does not recognize community property. The failure of the Treasury Department to address itself to the above situation does not warrant the lower court's conclusion that this meant that the federal authorities consider an election

as to self-employment income to be irrelevant as to the right to file joint or separate federal income tax returns.

The lower court's ruling would permit the assignment of income, not only as to a husband and wife, but also as to strangers owning property in joint tenancy. The Internal Revenue Code as enacted does not provide for the assignment of income for purposes of reducing tax liabilities, and the adoption of the Internal Revenue Code and the interpretations thereof by the State of North Dakota through federalizing therefor should restrict the assignment of income for state income tax purposes. This requires the proper interpretation of federal statutes and application thereof by the state courts.

## CONCLUSION

It is not only the Petitioner, but thousands of North Dakota taxpayers, including husbands and wives, owning property in joint tenancy and deriving income therefrom, and their tax advisors, that are asking this Court, as our Court of last resort, under exceptional circumstances necessitated by justice and equity, to issue a Writ of Certiorari to the Supreme Court of North Dakota, or remand same back to the Court below with the directive to reconsider the federal question presented and to make a written decision thereon.

Dated this 18th day of April, 1975, at Bismarck, North Dakota.

Respectfully submitted,

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